



Quality Control standards at firm and engagement level SQC 1 and SA 220

**Organised by PEER REVIEW BOARD
Hosted by ICAI Nagpur Branch**

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Applicability and Objectives

- Effective for audits of financial statements for periods beginning on or after April 1, 2009
- Firm's responsibilities for its system of quality control for audits and reviews of historical financial information and other assurance and related engagements
- Responsibilities of engagement personnel for specific types of engagements are covered in SA 220 – effective from April 1, 2010
- The firm should establish a system of quality control designed to provide it with reasonable assurance that the;
 - Firm and its personnel comply with professional standards, regulatory and legal requirements, and
 - that reports issued by the firm or engagement partner(s) are appropriate in the circumstances
- SQC 1 is to be read in conjunction with the requirements of the Chartered Accountants Act, 1949, the Code of Ethics and any other relevant pronouncement of the Institute and relevant legal or regulatory requirement

IT APPLIES TO ALL THE FIRMS

Elements of System of Quality Control

- Leadership responsibilities for quality within the firm.
- Ethical requirements.
- Acceptance and continuance of client relationships and specific engagements
- Human Resources
- Engagement Performance
- Monitoring

DOCUMENTATION OF EVIDENCE OF OPERATION OF EACH OF THE ELEMENTS OF CONTROL

MANNER OF DOCUMENTATION DEPENDS ON THE SIZE AND COMPLEXITY OF PRACTICE AND ORGANISATION

Leadership responsibilities for Quality within the firm.

- Ultimate responsibility with firm's CEO or Managing Partner – why?
 - Commercial consideration
 - Performance evaluation
 - Allocation of resources
- Precautions to be taken if operational responsibilities are delegated
- How do you Communicate? -
 - Training Seminars. Meetings, Formal or informal dialogue, Mission Statements, Newsletters, Briefing Memoranda,
 - Demonstrate through partner and staff appraisal procedures

Leadership responsibilities for Quality within the firm.

Ultimate responsibility of the Managing Partner	<ul style="list-style-type: none">▪ Design, implementation and operating effectiveness of quality control▪ Educating professional personnel
Commercial considerations do not override the quality	<ul style="list-style-type: none">▪ MP to continually evaluate client relationships and specific engagements▪ Emphasising to personnel that fee considerations and scope of service should not infringe quality control
Responsibility assigned to appropriate personnel	<ul style="list-style-type: none">▪ MP to designate a Quality Control Partner▪ <i>In case of sole proprietorship, sole practitioner is the Quality Control partner</i>
Performance evaluation, compensation and advancement	<ul style="list-style-type: none">▪ Compensation system to take into consideration firm's feedback and reward partners and personnel for audit quality
Allocation of appropriate resources for quality control	<ul style="list-style-type: none">▪ Designated QC to be provided sufficient time and resources▪ QC documentation to be provided to personnel▪ Timely review of QC policies

Ethical Requirements

- Fundamental Principles include
 - Integrity
 - Objectivity
 - Professional competence and care
 - Confidentiality
 - Professional behavior
- Conceptual approach to independence for assurance engagements including aspects such as threats to independence, accepted safeguards and the public interest

Independence

- Generally recognized threat to independence:
 - Familiarity threat
 - Self review threat
 - Intimidation threat
 - Advocacy threat
 - Conflict of interest

Ethical Requirements

Personnel adherence to ethical requirements	<ul style="list-style-type: none">▪ MP to designate Independence and Ethics partner and empowering him/her▪ Establishing system for identifying all services performed for all clients▪ Regularly consulting ICAI's journal and website▪ Ensuring training attendance <p><i>In case of sole proprietorship, sole practitioner is the Independence and Ethics partner</i></p>
Establish procedures to communicate independence requirements	<ul style="list-style-type: none">▪ People prohibited from having financial or business relationship▪ List is easily available and updated promptly▪ Providing frequent reminders
Establish procedures to identify and evaluate possible threats to independence	<ul style="list-style-type: none">▪ Partner to consider relevant information about client engagements▪ Providing training to partners and professional staff▪ Accumulating and communicating information▪ Personnel to promptly report threats to independence▪ Communicating identified breaches and corrective actions▪ Periodic review of unpaid fees from clients▪ Documenting the threats and safe-guards applied

Ethical Requirements

Withdraw if safeguard to reduce threats to independence to an acceptable level cannot be applied

- Consulting within firm and legal counsel
- Consider regulatory requirements

Obtain written confirmation at least annually of compliance on independence

- Review representations and resolve reported exceptions
- Audit??

Establish procedures for confirmation of independence of another firm performing part of engagement

- Using practice aids prescribing form and content of independence representations

Independence

- Involving an additional partner who is not associated with the audit engagement
- Rotation of senior partners or professional staff
- Discussing independence issues with the auditee's audit committee
- Withdrawing an individual from an audit, when that individual's economic or financial interests create a threat to independence
- Withdrawal from an engagement if safeguards to reduce threats to independence to an acceptable level cannot be applied
- Annual written confirmation, of compliance with firm's policies and procedures on independence
- Procedures for confirming the independence of another Firm that performs part of the engagement

Acceptance/Continuation - Client Relationship/Engagements

- Integrity of client
 - Reason for change
 - Owners, KPMs, Related Parties, TCWG
 - Business operations and practices
 - Attitude - Interpretation of accounting standards & Internal Controls
 - Fee levels
 - Past experience
 - Nature and purpose of services to be provided and management's understanding thereof
 - Inquiries with third parties who have business relationship
 - Annual reports and other publicly available information including search on digital media

Acceptance/Continuation - Client Relationship/Engagements

- Risk associated with providing services
 - Insistence for low fees
 - Limitation in scope of work
 - Evaluating risk of providing services to significant clients or other clients for which firm's objectivity/appearance may be impaired
- Competency, Capability, Time and Resources
 - Knowledge and expertise to complete the engagement
 - Sufficient people with incl specialist and EQCR are available
 - Timeline will be achieved
- Approval of MP for client acceptance
- Compliance with ethical requirements
- What if information received subsequent to acceptance?

Acceptance/Continuation - Client Relationship/Engagements

- Client continuation
 - Business changes, KMPs leaving, Delinquency in paying fees
 - Decision to exit certain industry
 - Difficulty in replacing people
 - Prior recommendation not addressed - eg weakness in internal control not addressed
 - Going concern
- Policy to obtain understanding with client regarding services to be performed – Engagement letter
- Procedure for withdrawal from engagement or both engagement and client relationship

DOCUMENTATION ABOUT CLIENT/ENGAGEMENT ACCEPTANCE, CONTINUATION, DISCONTINUATION INCLUDING APPROVALS

Human Resources

The Firm's policies and procedures should be designed to provide it with reasonable assurance that

- it has sufficient personnel with the capabilities and competence,
- the personnel are committed to ethical principles necessary to perform its engagements in accordance with professional standards and regulatory and legal requirements
- Enable the Firm or engagement partners to issue reports that are appropriate in the circumstances

Human Resources

- Estimation of personnel needs
- Competency and Capability
- Recruitment
- Performance evaluation
- Compensation
- Promotion
- Career Development

Human Resources

Personnel who are hired possess the characteristics that enable them to perform competently.

- Designate individual for managing this function, evaluating firm's needs and developing criteria for interviewing and hiring
- Establish understanding amongst partners about the qualifications, attributes, achievements and experiences desired in entry-level and experienced personnel.
- Other procedures for hiring like background checks etc.

Human Resources

Assign personnel (including partners) based on the knowledge, skills, and abilities required in the circumstances and the nature and extent of supervision needed

- Assigning personnel based on engagement type, size, complexity, risk profile
- Designating partner to be responsible for each engagement
- MP approval in case of high-risk engagements

Personnel participate in general and industry-specific continuing professional education and development (CPED) activities that enable them to accomplish assigned responsibilities

- Assigning responsibility to partner to maintain CPED
- Encouraging participation at each level
- Communicating and distributing to personnel changes in accounting, auditing and QC standards

Personnel selected for advancement have the qualifications to fulfill the responsibilities they will be called on to assume

- Assigning responsibility to partner to establish criteria for evaluating personnel, inform personnel on criteria for advancement
- Counselling personnel on progress and career opportunities
- Evaluating partners periodically by counselling, peer evaluation or self appraisal

Engagement Performance

- Design policies & procedures to provide reasonable assurance that;
 - Engagements are performed in accordance with professional standards and regulatory and legal requirements
 - Firm or partner issues reports that are appropriate in the circumstances
- Establish consistency in quality of engagement performance
- Easily accessible to people
- Mainly includes Planning, Directing, Supervision, Review, Consultation, EQCR
- Processes to keep all policies and procedures current.

Engagement Performance - Planning

Planning for engagements meets professional, regulatory, and the Firm's requirements.

- The Firm implements this policy by maintaining and providing personnel with the Firm's practice aids that prescribe the factors the engagement team should consider in the planning process for an engagement and the extent of documentation of those considerations.
- Planning considerations may vary depending on the size and complexity of the engagement.
- Planning activities – well planned is half done

Engagement Performance - Planning

- How engagement teams are briefed on the engagement to obtain an understanding of the objectives of their work.
- Processes for complying with applicable engagement standards.
- Processes of engagement supervision, staff training and coaching.
- Methods of reviewing the work performed, the significant judgments made and the form of report being issued.
- Appropriate documentation of the work performed and of the timing and extent of the review.

Review and Supervise

The engagement is **performed, supervised, documented, reported and communicated** in accordance with the requirements of professional standards, applicable regulatory requirements, and the Firm's standard.

- Ensure compliance with auditing standards
- Adequate supervision considering the ability & experience of team members
- Tracking the progress of the engagement
- Addressing significant risk identified and new risk during execution and update on planned approach
- Controls and substantive approach
- Significant issues identified during the engagement and its resolution
- Identifying matters for consultation or consideration by more experienced engagement team members

Review and Supervise

- Appropriate consultations and conclusion are documented
- Nature, timing and extent of work performed is adequate or needs revision
- Work performed supports the conclusion and is documented
- Evidence obtained in support of financial statement assertions and disclosures is sufficient and appropriate
- Objectives of engagement procedures have been achieved

Consultation

Establish policies & procedures to provide reasonable assurance that;

- Appropriate consultation takes place on difficult or contentious matters
- Sufficient resources are available to enable appropriate consultation to take place
- Nature and scope of such consultations are documented
- Conclusions resulting from consultations are documented and implemented

Consultation

Requiring consultation in specialized areas or situations with appropriate individuals within and outside the Firm when matters such as the following arise:

- The application and interpretation of technical pronouncements.
- Industries with special accounting, auditing, or reporting requirements.
- Emerging practice problems.
- Choices among alternative generally accepted accounting principles.
- Re-issuance of a report, consideration of omitted procedures after a report has been issued, or subsequent discovery of facts that existed at the date a report was issued.
- Filing requirements of regulators.
- Meetings with regulators at which the Firm is to be called on to support the application of generally accepted accounting principles or generally accepted auditing standards that have been questioned.

Consultation

- Consultation uses appropriate research resources as well as the collective experience and technical expertise of the firm
- A firm needing to consult externally, for example, a firm without appropriate internal resources, may take advantage of advisory services provided by
 - other firms, or
 - professional and regulatory bodies
- The documentation is sufficiently complete and detailed to enable an understanding of
 - The issue on which consultation was sought; and
 - The results of the consultation, including any decisions taken, the basis for those decisions and how they were implemented

GIVE FULL FACTS AND KEEP ENOUGH TIME FOR CONSULTATION

Engagement Quality Control Review (EQCR)

- Mandatory for all audits of financial statements of Listed entities
 - Is limited review covered?
- Specify criteria for other audits (unlisted) requiring EQCR e.g.
 - Public Interest
 - Unusual or higher risk
 - Laws and regulations requiring EQCR
- Require EQCR for all audits of unlisted entities meeting specified criteria

COMPLETION OF EQCR BEFORE THE ISSUANCE OF REPORT

Engagement Quality Control Review (EQCR)

- The firm's policies and procedures should require the completion of the engagement quality control review before the report is issued
- The firm should establish policies and procedures setting out :
 - The nature, timing and extent of an engagement quality control review
 - Criteria for the eligibility of engagement quality control reviewers
 - Documentation requirements for an engagement quality control review
- Criteria for eligibility
 - Technical qualifications required to perform the role, including the necessary experience and authority; and
 - The degree to which an engagement quality control reviewer can be consulted on the engagement without compromising the reviewer's objectivity.
 - In case of listed company – experience and authority to act as an engagement partner

EQCR – Nature, Extent and Timing

- Independence – Firm and Engagement Team
- Significant Risk identified
- Judgements
- Consultation
- Significant issues identified and its resolution
- Corrected and Uncorrected misstatements
- Matters to be communicated to Management, TCWG and Regulators
- Review of selected work papers
- Report and other deliverables
- Extent depends on complexities and risk

TIMELY INVOLVEMENT IS A MUST

Eligibility to be EQCR

- The firm's policies and procedures are designed to maintain the objectivity of EQCR.
- EQCR
 - Is not selected by the engagement partner
 - Does not otherwise participate in the engagement during the period of review
 - Does not make decisions for the engagement team
 - Is not subject to other considerations that would threaten the reviewer's objectivity

Suitably qualified external persons may be contracted where sole practitioners or small firms identify engagements requiring engagement quality control reviews. Alternatively, some sole practitioners or small firms may wish to use other firms to facilitate engagement quality control reviews.

EQCR - Documentation

Policies and procedures on documentation of the engagement quality control review should require documentation that:

- The procedures required by the firm's policies on engagement quality control review have been performed;
- The engagement quality control review has been completed before the report is issued; and
- The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the engagement team made and the conclusions they reached were not appropriate.

Difference of Opinion

- Policies and Procedures of dealing with difference of opinion between;
 - Engagement team and those consulted
 - Engagement Partner and EQCR
- Steps to be followed to resolve differences

NO REPORT SHOULD BE ISSUED TILL DIFFERENCES ARE RESOLVED

Engagement Documentation – Completion and Archival

Policies and procedures for engagement teams to complete the assembly of engagement files on a timely basis post the issuance of engagement reports

- In case of audit normally 60 days
- When two or more reports are issued? Eg as component auditor and as statutory auditor on a stand-alone basis

Confidentiality, Safe Custody and Retrieval

- Policies and procedures designed to maintain the confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation
- Determination of when and by whom engagement documentation was created, changed or reviewed;
- Protect the integrity of the information at all stages of the engagement,
- Prevent unauthorized changes to the engagement documentation; and
- Allow access to the engagement documentation by the engagement team and other authorized parties as necessary to properly discharge their responsibilities.

Engagement Documentation – Retention

- Retention of engagement documentation for a period sufficient to meet the needs of the firm or as required by law or regulation.
- Enable the retrieval of, and access to, the engagement documentation during the retention period, particularly in the case of electronic documentation since the underlying technology may be upgraded or changed over time.
- Provide, where necessary, a record of changes made to engagement documentation after the engagement files have been completed.
- Enable authorized external parties to access and review specific engagement documentation for quality control or other purposes.

ENGAGEMENT DOCUMENTATION IS THE PROPERTY OF THE FIRM

Monitoring

- Policies and procedures designed to provide it with reasonable assurance that
 - The policies and procedures relating to the system of quality control are relevant, adequate, operating effectively and complied with in practice.
 - Ongoing consideration and evaluation of the firm's system of quality control, including a periodic inspection of a selection of completed engagements.

Monitoring - Purpose

The purpose of monitoring compliance with quality control policies and procedures is to provide an evaluation of:

- Adherence to professional standards and regulatory and legal requirements;
- Whether the quality control system has been appropriately designed and effectively implemented; and
- Whether the firm's quality control policies and procedures have been appropriately applied, so that reports that are issued by the firm or engagement partners are appropriate in the circumstances..

Monitoring

Assign responsibility for monitoring process	<ul style="list-style-type: none"> ▪ MP designates QC partner ▪ Identify need to; <ul style="list-style-type: none"> ▪ Revise policies and procedures if ineffective in inspection or inappropriately designed, ▪ Improve compliance with firm policies related to QC
Perform monitoring procedures sufficiently comprehensive to assess compliance with all applicable professional standards and QC policies	<ul style="list-style-type: none"> ▪ Assign partner/s to perform annual inspection ▪ Determine criteria for selection of samples – Listed/high risk accounts, all partners coverage, disagreements, complaints, first year clients etc ▪ Approach, timetable, documentation ▪ Decide period to retain inspection documentation ▪ Reviewing resolution to matters reported and recommended corrective actions ▪ Prepare summary inspection report for partner group
Communication of <ul style="list-style-type: none"> ▪ Deficiencies noted and recommendations for appropriate remedial action ▪ Results of monitoring of its QC system process to firm personnel at least annually 	<ul style="list-style-type: none"> ▪ Discussion of observations of inspection with partner ▪ Preparing summary report with recommended changes ▪ Reviewing recommended corrective actions and reaching final conclusions ▪ Communication to all personnel deficiencies noted

Monitoring

Preparing and retaining appropriate documentation providing evidence of operation of each element of its system of QC

- Designing summary monitoring report to include procedures for selecting completed engagements to be inspected
- Record of the evaluation
- Identification of deficiencies noted and further action

Dealing with complaints and allegations

- Assurance by MP to report without fear
- Partner not involved in the engagement to investigate complaints about failure to comply with professional/regulatory requirements or allegation of non compliance of firm's QC etc
- Documenting allegation and response to them

Monitoring

- To appoint Quality control partner
- To evaluate design and operating effectiveness of operation of control
- On going basis
 - Analysis of new development in professional standards and regulatory requirements on the system
 - Review of written confirmation of independence
 - Continuing professional development and training
 - Client/engagement acceptance
 - Corrective action to be taken or improvement in firm's policies and procedures
 - Communication of corrective action to be taken
 - Take in to account observations and comments of inspecting agencies/peer reviewer
 - Follow up for modification in firm's policies and procedures

Monitoring

- Surprise selection
- Atleast one engagement per partner over inspection cycle
- Basis of Inspection cycle
- Inspection by those not connected with the engagement and preferably from different office
- Small firms and sole proprietorship

Evaluation of Deficiencies

- Instances that do not necessarily indicate that the firm's system of quality control is insufficient to provide it with reasonable assurance that it complies with professional standards and regulatory and legal requirements, and that the reports issued by the firm or engagement partners are appropriate in the circumstances;

OR

- Systemic, repetitive or other significant deficiencies that require prompt corrective action.
- Taking remedial action in relation to individual engagement or personnel
- Training and development
- Changes in quality control policies and procedures
- Disciplinary action

Evaluation of Deficiencies

- What if report is may not be inappropriate or procedures were omitted
- Communicate findings to firm's leadership including managing partner

Re-inforcement of Firm's policies

The firm's policies and procedures should emphasize the fundamental principles to reinforced in particular by:



Thank You