

1

Quality Control

SQC - 1

“Quality Control for Firms that Perform Audits & Reviews of Historical Financial Information and Other Assurance & Related Services Engagements”

- Firm should establish a system of Q.C. designed to provide it with reasonable assurance that (a) firm & its personnel comply with professional standards & regulatory and legal requirements and (b) reports issued by firm or EP (s) are appropriate.
- Firm’s system of Q.C. should include policies and procedures addressing the following elements:

(a) Leadership responsibilities for quality within the firm.	(b) Ethical requirements.
(c) Acceptance & continuance of client relationships & engagements.	(d) Human resources.
(e) Engagement performance.	(f) Monitoring.

Leadership Responsibilities for Q.C.

- Establish policies & procedures designed to promote internal culture based on recognition that quality is essential in performing engagements.
- Such policies & procedures require firm CEO/managing partners, to assume ultimate responsibility for firm’s system of Q.C.
- Any person assigned operational responsibility for firm’s Q.C. system should have sufficient & appropriate experience & ability and necessary authority, to assume that responsibility.

Considerations while upholding quality of firm

- (i) Firm assigns its management responsibilities so that commercial considerations do not override quality of work performed.
- (ii) Firm’s policies and procedures in relation to its personnel are designed to demonstrate its overriding commitment to quality.
- (iii) Firm devotes sufficient resources for development & documentation of its QC policies & procedures.
- (iv) Firm before accepting an engagement should acquire vital information about client. Such information help firm to decide about integrity of Client, promoters & KPM, competence (including capabilities, time & resources) to perform engagement and compliance with ethical requirements.

Independence

Policies & procedures should enable:

- Communication of independence requirements to personnel & others.
- Identify and evaluate circumstances & relationships that create threats to independence.
- Take appropriate action for elimination of threats or reduce them to acceptable level/withdrawal from engagement.
- Promptly notify firm of circumstances and relationships that create a threat to independence, for appropriate action.

Other Points

- Firm should obtain Annual written confirmation as to compliance with independence requirements.
- Create policies to reduce Familiarity threat, e.g. rotation of EP atleast every 7 years in case of audit of listed entities.

Ethical Requirements

Establish policies & procedures to reasonable assure that Firm & personnel comply with relevant ethical requirements of:

1. Integrity.
2. Objectivity.
3. Professional competence & due care.
4. Confidentiality.
5. Professional behaviour.

Fundamental principles should be emphasized by:

- (a) Actions of the leadership of the firm
- (b) Spreading awareness and training
- (c) Monitoring
- (d) A process for dealing with non-compliance.

SQC - 1

“Quality Control for Firms that Perform Audits & Reviews of Historical Financial Information and Other Assurance & Related Services Engagements”

Client Acceptance/Continuance

Before accepting an engagement, Firm should acquire vital information about client. Such an information should help firm to decide about:

- (a) Integrity of Client, promoters and KMP.
- (b) Competence (including capabilities, time and resources) to perform engagement.
- (c) Compliance with ethical requirements.

Establish policies w.r.t. withdrawal from engagement that include the following:

- (a) Discussing with appropriate level of mngt. & TCWG regarding appropriate action that the firm might take.
- (b) If firm determines that it is appropriate to withdraw, discuss with mngt. & TCWG, withdrawal from engagement and reasons for withdrawal.
- (c) Considering whether there is any requirement for firm to report withdrawal to regulatory authorities.
- (d) Documenting significant issues, consultations, conclusions and the basis for the conclusions.

Considerations as to integrity of Clients

1. Identity & business reputation of principal owners, key mngt., related parties and TCWG.
2. Nature of client's operations, including its business practices.
3. Information concerning attitude of principal owners, key mngt. & TCWG towards matters as aggressive interpretation of ASs & IC environment.
4. Whether client is aggressively concerned with maintaining firm's fees as low as possible.
5. Indications of inappropriate limitation in scope of work.
6. Indications that client might be involved in money laundering or other criminal activities.
7. Reasons for proposed appointment and non-reappointment of previous firm.

Matters be considered to determine whether firm has capabilities, competence, time & resources to undertake engagement

1. Firm personnel have knowledge of relevant industries or subject matters;
2. Firm personnel have experience with relevant regulatory or reporting requirements, or ability to gain necessary skills & knowledge effectively;
3. Firm has sufficient personnel with necessary capabilities and competence;
4. Experts are available, if needed;
5. Individuals meeting the criteria and eligibility requirements to perform EQCR are available, where applicable; and
6. Firm would be able to complete engagement within reporting deadline.

Human Resources

Establish policies/procedures to assure that Firm has sufficient personnel with capabilities, competence & commitment to ethical principles.

- Identity & role of EP communicated to key members of client's management and TCWG;
- EP has appropriate capabilities, competence, authority & time to perform the role; and
- Responsibilities of EP clearly defined and communicated to that partner.

Engagement Performance

Important aspects of engagement performance

- Direction, Supervision and Review
- Consultation
- Differences of opinion
- Engagement Q. C. review (EQCR)
- Engagement documentation

Review

EP shall review work performed by team members and consider whether:

- (a) Work has been performed in accordance with professional standards and regulatory and legal requirements;
- (b) Significant matters have been raised for further consideration;
- (c) Appropriate consultations have taken place;
- (d) There is a need to revise the NTE of work performed;
- (e) Work performed supports the conclusions reached and is appropriately documented;
- (f) Evidences obtained are sufficient and appropriate to support the report; and
- (g) Objectives of engagement procedures have been achieved.

Consultation

- Consultation should take place in difficult matters pertaining to engagement and includes discussion with individuals within or outside the firm having specialized expertise.
- Complete and proper documentation should be maintained on issues involved and results of consultation.

Differences of opinion

- There might be difference of opinion within ET, with those consulted and between EP and EQC reviewer.
- Report should only be issued after resolution of such differences.

SQC - 1

“Quality Control for Firms that Perform Audits & Reviews of Historical Financial Information and Other Assurance & Related Services Engagements

Engagement Performance

EQCR

- Firm should establish policies and procedures that
 - (1) Require QC review for all audits of F.S. of listed companies.
 - (2) Require completion of engagement before QC review.
- EQC reviewer should be suitably qualified external person such as a partner or employee (who should be member of ICAI) or can be from another firm with similar background.
- Ensure objectivity of reviewer; participation in engagement or making decisions for ET is to be avoided at all costs.
- Firm’s policies should provide for replacement of EQC reviewer where ability to perform an objective review may be impaired.

Matters considered in EQCR for audit of F.S. of Listed Entities

- (1) ET evaluation of firm’s independence.
- (2) Significant risks identified during engagement & its responses.
- (3) Judgments made, particularly w.r.t. materiality and significant risks.
- (4) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult matters & conclusions reached.
- (5) Significance and disposition of corrected and uncorrected misstatements identified during engagement.
- (6) Matters to be communicated to mngt., TCWG & other parties.
- (7) Whether working papers selected for review reflect the work performed in relation to the significant judgments and support the conclusions reached.
- (8) Appropriateness of the report to be issued.

Engagement Documentation

- Establish policies & procedures for assembly of final engagement files on timely basis.
- Engagement files should be completed in not more than 60 days after date of auditor’s report.
- Establish policies & procedures to maintain confidentiality, safe custody, integrity, accessibility & retrievability of engagement documentation.
- Unless otherwise specified by law or regulation, engagement documentation is property of firm.
- Engagement documentation has to be retained for sufficient period; in specific case of audit engagements, retention period ordinarily is no shorter than 7 years from date of auditor’s report.

Monitoring

Establish Policies & procedures to reasonable assure that QC policies/ procedures are relevant, adequate, operating effectively, complied within practice.

Factors considered in monitoring of QC

- (i) Deciding whether QC system has been appropriately designed & effectively implemented.
- (ii) Examining whether new developments in professional standards, legal and regulatory requirements have been reflected in QC policies.
- (iii) Entrusting responsibility of monitoring to a partner or other persons with sufficient and appropriate experience and authority in firm.
- (iv) Dealing with complaints & allegations against firm or employees.
- (v) Taking remedial actions against personnel who did not conform to QC policies.
- (vi) Taking action when deficiencies in design or operation of QC policies and procedures, or non-compliance with QC system are identified.

Complaints and Allegations

- Firm should establish policies and procedures to deal appropriately with:
 - (a) Complaints & allegations that work performed by firm fails to comply with professional standards and regulatory and legal requirements; and
 - (b) Allegations of non-compliance with firm’s system of quality control.
- Complaints and allegations may originate from within or outside the firm; may be made by firm personnel, clients or others; may be received by ET members or other firm personnel.
- Firm shall investigate such complaints and allegations in accordance with established policies.
- Complaints, allegations and responses to them shall be documented.
- Where results of investigations indicate deficiencies in design or operation of firm’s Q.C. policies and procedures, or non-compliance with the firm’s system of quality control by an individual or individuals, firm shall take appropriate action.

SA – 220 “Quality Control for an audit of F.S.”

Objective: Implement QC Policies at Engagement Level that provide assurance that audit complies with Professional Standards & Regulatory & Legal Requirements and audit report issued is appropriate.

SA-220 is premised on the basis that the firm is subject to SQC 1.

Independence	<pre> graph LR A[Form a conclusion on compliance with applicable independence] --> B[Obtain relevant information from Firm] B --> C[Identify & Evaluate circumstances & Relationship that threatens independence] C --> D[Evaluate information on identified breaches.] D --> E[Determine if these threaten independence] E --> F[Take appropriate action to eliminate such threats or Promptly report inability to take appropriate action to firm.] </pre>
Acceptance / Continuance of Client relationship	<ul style="list-style-type: none"> Be satisfied that appropriate procedures regarding client acceptance/continuance have been followed. Determine whether conclusions reached are appropriate. If EP obtains information that would have caused firm to withdraw the engagement, communicate information promptly to firm. <div style="border: 1px solid black; padding: 5px; margin-top: 10px; text-align: center;"> <p style="color: red; margin: 0;">Examples of Information</p> <ol style="list-style-type: none"> <li style="color: red;">1. Integrity of Principal Owners, Mngt & TCWG <li style="color: red;">2. Competency of ET to perform engagement. <li style="color: red;">3. Availability of necessary capabilities, including time & resources. <li style="color: red;">4. Compliance with relevant ethical requirements. <li style="color: red;">5. Significant matters that arise during the current or previous audit engagement. </div>
Engagement Performance	<p>EP has the responsibility for the following:</p> <ol style="list-style-type: none"> (a) Direction, supervision and performance of audit engagement; (b) Issue of appropriate Auditor’s report. (c) Review of audit documentation before issue of audit report. (d) Ensuring that SAAE has been obtained to support the conclusions reached. (e) Undertaking appropriate consultation on difficult matters. <div style="background-color: yellow; text-align: center; padding: 2px; margin: 5px 0;">Engagement Quality Control Review (EQCR)</div> <p>For audits of F.S. of listed entities, EP shall:</p> <ol style="list-style-type: none"> (a) Determine that an EQC Reviewer has been appointed. (b) Discuss significant matters arising during the audit engagement. (c) Not date the auditor’s report until the completion of the EQCR. <p>Matters to be evaluated by EQC Reviewer:</p> <p>EQC reviewer shall perform an objective evaluation of significant judgments made by ET, and the conclusions reached in formulating the auditor’s report. This evaluation shall involve:</p> <ol style="list-style-type: none"> (a) Discussion of significant matters with the EP; (b) Review of the F.S. and the proposed auditor’s report; (c) Review of selected audit documentation relating to the significant judgments; and (d) Evaluation of conclusions reached in formulating the auditor’s report and consideration of whether the proposed auditor’s report is appropriate. <p>Additional Considerations in audit of F.S. of Listed Entities:</p> <ul style="list-style-type: none"> ET’s evaluation of firm’s independence in relation to audit engagement. Whether appropriate consultation has taken place on matters involving differences of opinion/difficult matters & conclusions arising from consultations. Whether audit documentation selected for review reflects the work performed w.r.t. significant judgments made & supports the conclusions reached.

SQC 1 vs. SA 220

SQC 1	SA 220
SQC 1 applies to entire firm & fixes responsibility of firm to be assumed by CEO or Managing Partners.	SA 220 applies to particular audit engagement & EP takes responsibility of the same.
SQC 1 is applicable to audits, reviews of historical financial Information, other assurance & related services engagements.	SA 220 is applicable to audit engagements only.
SQC 1 relates to setting up of a quality control system consisting of policies and procedures for firm as a whole.	SA 220 deals with ET responsibilities to implement QC procedures that are applicable to audit.
SQC 1 pertains to establishing a system of QC designed to provide firm with a reasonable assurance that a firm and its personnel comply with professional standards & regulatory & legal requirements so that reports issued by firm/EPs are appropriate.	SA 220 is premised on the basis that firm is subject to SQC 1. Therefore, SQC 1 is a <i>sine qua non</i> for applicability of SA 220.

Mechanism for Review of Quality Control

Peer Review Board (PRB)	<p>Constituted by Council. Objective is to ensure that, in carrying out assurance assignments:</p> <p>(a) Technical, professional & ethical standards including regulatory requirements are complied with by members of ICAI.</p> <p>(b) Proper systems are in place including documentation thereof.</p> <p>Once a PU is subjected to Peer review, its assurance engagement records are subject to examination & review by Peer Reviewer. On completion, "Peer Review Certificate" is issued in case of unqualified report. In case of qualified report, it is informed to PU that same cannot be issued along with reasons therefor as well as inform about due date for conducting a follow-on review as decided by the Board.</p>
Quality Review Board (QRB)	<ul style="list-style-type: none"> • Set up by C.G., and consists of members nominated by C.G. & Council of ICAI. • Functions of QRB are: <ul style="list-style-type: none"> (a) To make recommendations to Council regarding quality of services provided by members; (b) To review quality of services provided by members including audit services; and (c) To guide members to improve quality of services and adherence to statutory and other regulatory requirements. • Statutory auditors are identified for their audit quality review based upon risk-based approach and Review is carried out by technical reviewers (empanelled by QRB).
NFRA	<ul style="list-style-type: none"> • Constituted in terms of Sec. 132(1) of Companies Act, 2013. • Duties of NFRA include the following: <ul style="list-style-type: none"> (a) Monitor & enforce compliance with ASs and auditing standards. (b) Oversee quality of service of associated professions. • NFRA also has power to undertake investigation of auditors of listed companies, insurance and banking companies and other companies as provided for in Rule 3 of NFRA Rules, 2018. • Overseeing quality of audit services of <u>listed companies</u> falls under purview of NFRA. QRB can review quality of audit services only in respect of entities other than those specified under Rule 3 of NFRA Rules & those referred to QRB by NFRA.

"Do the best you can, until you know better; Then when you know better, do better." — Maya Angelou