

Quality Management Standards and Compliance Audit Updates

New quality management standards are reshaping how firms oversee their audit practices — and this section breaks down exactly what those changes mean. You'll get a clear summary of the new QM standards and what each one does, along with a detailed look at amendments made by SAS No. 148 to AU-C 935 for compliance audits. Practitioners involved in firm quality control or performing compliance engagements will find this section especially relevant to their day-to-day work.

CREDIT HOURS 2 | FIELD OF STUDY AUDITING | EXAM QUESTIONS 10

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LEARNING ASSIGNMENTS AND OBJECTIVES

Assignment

- Study the full course materials included here.
- Complete the review questions after each chapter.
- Answer 10 final exam questions.
- Final exam is scored immediately, 70% or better passes.
- Certificate of completion is available in your account.
- Failed exams can be retaken free of charge.

Course Objectives

- Recall the date by which an engagement partner must take responsibility for determining that ethical requirements are fulfilled.
- Identify certain requirements an engagement partner must satisfy in performing an audit engagement.
- Recognize examples of resources assigned or made available by a firm to support performance of an audit engagement.
- Identify a type of unconscious bias defined in SAS No. 146.
- Recall a possible action that an engagement team may take to mitigate impediments to exercise professional skepticism.
- Identify when a successor auditor should request management to authorize a predecessor auditor's response to the successor auditor's inquiry.
- Recognize one of the new inquiries a successor auditor should make of a predecessor auditor by SAS No. 147.
- Recall the extent of a predecessor auditor's response to a successor auditor's inquiries when there are certain restrictions on the predecessor auditor.
- Identify an example of a recently issued auditing standard that SAS No. 148 incorporates into amendments to AU-C 935, Compliance Audits.

- Recognize one of the five components of a system of internal control identified in SAS No. 145 and incorporated into AU-C 935 by SAS No. 148 amendments.
- Recall examples of inherent risk factors related to identifying and assessing risks of material misstatement in a compliance audit.
- Identify the party required to take overall responsibility for the quality on a group audit engagement in accordance with SAS No. 149.

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Section 1

Chapter Objective

After completing this assignment, you should be able to:

- Recall the date by which an engagement partner must take responsibility for determining that ethical requirements are fulfilled.
- Identify certain requirements an engagement partner must satisfy in performing an audit engagement.
- Recognize examples of resources assigned or made available by a firm to support performance of an audit engagement.
- Identify a type of unconscious bias defined in SAS No. 146.
- Recall a possible action that an engagement team may take to mitigate impediments to exercise professional skepticism.
- Identify when a successor auditor should request management to authorize a predecessor auditor's response to the successor auditor's inquiry.
- Recognize one of the new inquiries a successor auditor should make of a predecessor auditor by SAS No. 147.
- Recall the extent of a predecessor auditor's response to a successor auditor's inquiries when there are certain restrictions on the predecessor auditor.
- Identify an example of a recently issued auditing standard that SAS No. 148 incorporates into amendments to AU-C 935, Compliance Audits.
- Recognize one of the five components of a system of internal control identified in SAS No. 145 and incorporated into AU-C 935 by SAS No. 148 amendments.
- Recall examples of inherent risk factors related to identifying and assessing risks of material misstatement in a compliance audit.
- Identify the party required to take overall responsibility for the quality on a group audit engagement in accordance with SAS No. 149.

SAS NO. 146: QUALITY MANAGEMENT FOR AN ENGAGEMENT CONDUCTED IN ACCORDANCE WITH GAAS

Issued: June 2022 **Effective Date:** SAS No. 146 is effective for engagements conducted in accordance with GAAS for periods beginning on or after December 15, 2025.

Objective of SAS No. 146

The objective of SAS No. 146 is to provide guidance on quality management of an audit engagement.

General

In June 2023, the Auditing Standards Board (ASB) and the Accounting and Review Services Committee issued four interrelated final standards on quality management (collectively, QM standards):

- Statement on Quality Management Standards (SQMS) No. 1, *A Firm's System of Quality Management*
- SQMS No. 2, *Engagement Quality Reviews*
- SAS No. 146, *Quality Management for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards*
- SSARS No. 26, *Quality Management for an Engagement Conducted in Accordance with Statements on Standards for Accounting and Review Services*

SQMS Nos. 1 and 2, SAS No. 146, and SSARS No. 26 are collectively referred to as the “*quality management standards*.”

The new Quality Management (QM) Standards affect all firms that perform accounting and auditing engagements under the SASs, SSAEs, and SSARSs, starting in 2025 and 2026.

Collectively, the new standards do the following:

- Offer a new risk-based approach, incorporating a risk assessment process, driving firms to focus on quality management tailored to their circumstances
- Provide revised components of the system of quality management — two new components, including information and communication
- Include more robust leadership and governance requirements
- Require enhanced monitoring and remediation processes, and
- Establish new requirements for networks and service providers.

The new QM standards affect every firm that performs engagements in accordance with the SASs, SSAEs, or SSARSs.

Details of each of the standards follow.

Comparison of New QM Standards with Previous Standards

Standard	What It Replaces
SQMS No. 1, A Firm's System of Quality Management, and SQMS No. 2, Engagement Quality Reviews	Replaces existing SQCS No. 8, A Firm's System of Quality Control (QC sec. 10).
SSARS No. 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 and to be consistent with the changes made by SAS No. 146.
SAS No. 146, Quality Management for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards	Updates and supersedes AU-C 200, Quality Control for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards, to conform with SQMS No. 1 and 2.

Summary of QM Standards

New QM Standard	What It Does
SQMS No. 1: <i>A Firm's System of Quality Management</i>	Requires a firm to design, implement, and operate a system of quality management that is customized for the nature and circumstances of its accounting and auditing practice. It consists of: • <u>Eight components</u> that operate in an iterative and integrated manner. • Other requirements that address the roles and responsibilities for the system, leadership's overall evaluation of the system, network requirements or network services, and documentation. SQMS No. 1 introduces a <u>new risk-assessment process</u> aimed at achieving quality objectives. The firm is required to establish prescribed quality objectives, assess quality risks, and design and implement responses. SQMS No. 1 requires the firm leadership to annually evaluate and conclude whether the system of quality management is meeting its objectives. Systems of quality management in compliance with SQMS No. 1 are required to be <u>designed and implemented by December 15, 2025</u>, and the evaluation of the system of quality management is required to be performed within one year following December 15, 2025.

SQMS No. 2: <i>Engagement Quality Reviews</i>	Addresses the appointment and eligibility of the engagement quality reviewer and performance of engagement quality reviews. SQMS No. 2 <u>only applies</u> when the firm decides that an engagement quality (EQ) review is an appropriate response to a quality risk. SQMS No. 2 addresses the appointment and eligibility of the engagement quality reviewer and performance of engagement quality reviews. Eligibility requirements for EQ reviewers include: • Considering threats to objectivity but no cooling-off period required • Sufficient time to perform the EQ review, and • Permitted use of qualified external EQ reviewers and assistants. Performance of EQ reviews involves: • Focus on significant matters and significant judgments, and • Involvement of EQ reviewer at appropriate points in time throughout engagement. SQMS No. 2 is effective for audits or reviews of financial statements for <u>periods beginning on or after December 15, 2025</u>, and other engagements in the firm's accounting and auditing practice beginning on or after December 15, 2025.
SAS No. 146, <i>Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards</i>	SAS No. 146: • Clarifies and strengthens the <u>key elements of quality management</u> at the engagement level. • Focuses on the <u>important role of the engagement partner</u> in managing and achieving quality on the audit engagement. • Reinforces the importance of quality to <u>all members of the engagement team</u>. • Encourages proactive management of quality at the engagement level by emphasizing <u>the importance of the exercise of professional skepticism</u>, enhancing the documentation of the auditor's judgments, and reinforcing the need for robust communications during the audit, and • Addresses how the engagement partner leverages the firm's system and manages quality at the engagement level.

	SAS No. 146 makes clear that the <u>engagement partner has overall responsibility</u> for managing and achieving quality. SAS No. 146 becomes effective for audits of financial statements for <u>periods beginning on or after December 15, 2025</u>.
SSARS No. 26, <i>Quality Management for an Engagement Conducted in Accordance With Statements on Standards for Accounting and Review Services</i>	SSARS No. 26 amends AR-C 60, 70, 80, and 90 to conform the SSARSs to the new requirements made by SQMS Nos. 1 and 2. The SSARS No. 26 amendments: • Enhance certain concepts related to quality management for engagements performed in accordance with SSARSs. • Ensure that certain concepts related to quality management, where appropriate, are consistent between auditing standards (SAS No. 146) and the SSARSs. • Include a technical revision to paragraph .16 of AR-C 90 regarding the timing of obtaining an engagement letter to make it consistent with other SSARS sections (AR-C 70, 80, and 120), and with auditing and attestation standards. All the amendments made by SSARS No. 26 (except paragraph .16 of AR-C 90) are effective for SSARS engagements performed for <u>periods beginning on or after December 15, 2025 (calendar 2026 year end engagements)</u>. The amendment to paragraph .16 of AR-C 90 found in paragraph 5 of SSARS No. 26 is effective upon issuance.
Source: AICPA as modified by the author.	

Overview of SAS No. 146

SAS No. 146:

- Clarifies and strengthens the key elements of quality management in an audit engagement at the engagement level
- Focuses on the important role of the engagement partner in managing and achieving quality on the audit engagement
- Reinforces the importance of quality to all members of the audit engagement team.
- Encourages proactive management of quality at the engagement level by emphasizing the importance of the exercise of professional skepticism, enhancing the documentation of the auditor's judgments, and reinforcing the need for robust communications during the audit, and
- Addresses how the engagement partner leverages the firm's system and manages quality at the engagement level.

SAS No. 146 makes clear that the engagement partner has overall responsibility for managing and achieving quality in the audit engagement.

SAS No. 146 becomes effective for audits of financial statements for periods beginning on or after December 15, 2025 (calendar year 2026).

The Firm's System of Quality Management and the Role of Engagement Teams

1. Under SQMS No. 1, A Firm's System of Quality Management, the objective of the firm is to design, implement, and operate a system of quality management for engagements performed by the firm in its accounting and auditing practice that provides the firm with reasonable assurance that:
 - a) The firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements, and
 - b) Engagement reports issued by the firm or engagement partners are appropriate in the circumstances.
2. The engagement team, led by the engagement partner, is responsible, within the context of the firm's system of quality management and through complying with the requirements of this SAS, for the following:
 - a) Implementing the firm's responses to quality risks (that is, the firm's policies or procedures) that are applicable to the audit engagement using information communicated by, or obtained from, the firm
 - b) Given the nature and circumstances of the audit engagement, determining whether to design and implement responses at the engagement level beyond those in the firm's policies or procedures, and
 - c) Communicating to the firm information from the audit engagement that is required by the firm's policies or procedures to be communicated to support the design, implementation, and operation of the firm's system of quality management.

Complying with the requirements in other AU-C sections may provide information that is relevant to quality management at the engagement level.

The Engagement Partner's Responsibilities

The engagement partner is ultimately responsible and accountable for compliance with the requirements of SAS No. 146. In doing so, the engagement partner may seek assistance from others to fulfill these responsibilities.