

AGENDA PAPER

Item Number: 7
Date of Meeting: 6 September 2021
Subject: Proposed revisions to APES 320 *Quality Control for Firms*

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Purpose

To:

- provide the Board with Technical Staff's assessment of options for APES 320 *Quality Control for Firms* (extant APES 320) and APES 325 *Risk Management for Firms* (APES 325);
- obtain the Board's approval:
 - subject to the Board's review comments and editorials, to issue an Exposure Draft on proposed revisions to APES 320;
 - to change the name of APES 320 to *Quality Management for Firms that provide Non-Assurance Services*; and
 - of Technical Staff's proposed way forward for APES 320 and APES 325.

Background

The IAASB issued the final pronouncements for ISQM 1 *Quality Control for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance and Related Services Engagements* ([ISQM 1](#)), ISQM 2 *Engagement Quality Reviews* ([ISQM 2](#)) and ISA 220 *Quality Management for an Audit of Financial Statements* ([ISA 220](#)) in December 2020 (all operative on 15 December 2022).

ISQM 1 and 2 will replace ISQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* (ISQC 1). Extant APES 320 incorporates ISQC 1 with minor wording changes and additional AUST paragraphs to accommodate Australian legislation and environment. ISQM 1 and 2 fundamentally change how firms manage quality for audits, reviews, other assurance, and related services engagements.

An update was provided at the [March 2021 Board meeting](#), and the Board discussed two options to manage the impact of ISQM 1 and 2 on extant APES 320 and APES 325. The [Board approved Option 2](#) for APES 320 to be developed into a specific quality management standard

for firms providing non-assurance services while maintaining consistency with the firm-level components of the international quality management standards.

A further update was provided at the [June 2021 Board Meeting](#) on the release of [ASQM 1](#) and [ASQM 2](#) by the AUASB on 10 March 2021 (effective 15 December 2022) and Technical Staffs' engagement with the professional bodies on the proposed approach.

The Board considered a [preliminary draft exposure draft for APES 320](#) (Proposed June 2021 ED), including revisions for a quality management standard specific to non-assurance services using relevant extant requirements to minimise disruption for firms and alignment with ASQM 1 components. The [Board requested](#) Technical Staff to undertake further work to investigate and review:

- the proposals from the perspective of large, medium and small firms and consider how to make the standard simpler and less complex for small practices; and
- the impact of those investigations on APES 320 and APES 325 and to develop an action plan to be discussed at an out-of-session Board meeting.

An out-of-session Board meeting was convened on 16 August 2021 to discuss Technical Staff's proposed action plan for APES 320.

Key Considerations

Possible Options for APES 320 and APES 325

Technical Staff reviewed and investigated options to make APES 320 and APES 325 more relevant to non-assurance services, easier to navigate for firms of all sizes and simpler for smaller firms. Arguments for and against the following options are set out in Agenda Item 7(a):

- Option 1 – Redraft APES 320 *Quality Management for Firms* based on extant APES 320, restructured and focused on non-assurance services, with improved navigation for firms of all sizes and high-level alignment with ASQM 1.
- Option 2 – Create a new quality management standard for firms providing non-assurance services and not based on extant APES 320.
- Option 3 – Adopt option 1 to enable firms to update their quality management systems for non-assurance services simultaneously with changes required for ASQM 1 and then undertake a separate long-term project to refine and potentially further simplify APES 320.
- Option 4 – Explore the interaction between APES 320 and APES 325 and incorporating APES 320 into APES 325 or consolidate the two standards.

Technical Staff believe Option 1 is the most appropriate option for APESB to pursue as it:

- minimises disruption, including for small and medium practices (SMPs) in maintaining much of existing policies and procedures and systems (given that there is no evidence that existing quality control systems are not working for non-assurance services);
- provides high-level alignment for hybrid firms that provide assurance (subject to ASQM 1) and non-assurance services (subject to APES 320); and
- maintains in the public interest well established robust frameworks developed over decades.

Summary of proposed changes to the Preliminary Exposure Draft for APES 320 for Option 1

Technical Staff critically analysed the structure of APES 320 and the necessity of the requirements included in the Proposed June 2021 ED. As a result, Technical Staff have made significant changes to make the standard easier to navigate for firms of all sizes, more specific to non-assurance services and reduced requirements, making it simpler for SMPs.

The standard has been reduced by four pages, and requirement paragraphs have been reduced from 37 to 26 from the Proposed June 2021 ED. Of the 26 requirements, 19 are directly from extant APES 320, 5 are partially from extant APES 320 with some aspects derived from ASQM 1, and 2 are new paragraphs derived from ASQM 1. A further 13 sub-requirements have been either removed or changed to guidance material.

Agenda Item 7(b) details the changes made to the Proposed June 2021 ED, which includes:

- removing assurance based language including Reasonable Assurance, Engagement Quality Review(er), Relevant Ethical Requirements and Suitably Qualified External Person;
- restructuring Section 3 to clarify the firm's responsibility to establish and maintain a system of quality management, what the system consists of and the allocation and possible delegation of responsibilities;
- enhanced guidance on sources of information regarding acceptance and continuance of client relationships to include ethical letters and multiple sources such as the internet and industry forums;
- including a high-level requirement for sufficient and appropriate resources, maintaining extant human resources requirements and application material, removing requirements and simplifying guidance material for technological and intellectual services and service providers;
- including guidance referring to APES GN 30 *Outsourced Services* and its focus on the outsourcing agreement, performance management and monitoring relevant to outsourced services and service providers even if not an outsourced service;
- significant simplification of the information and communication requirement and associated guidance material;
- including guidance on the use of electronic signatures assisting in completing engagement files in a timely basis;
- consolidating and simplifying monitoring and remediation and including guidance on whistleblowing; and
- removing various other requirements, including in relation to professional standards and high-risk engagements.

The above changes are incorporated into Proposed Exposure Draft APES 320 ED 05/21 (Agenda Item 7(c)). Technical Staff have also updated the *Table mapping proposed APES 320 to extant APES 320* (Agenda Item 7(d)), including cross-references to proposed and extant paragraphs, high-level reasons for changes to extant paragraphs or inclusion of new material and notes all extant assurance related paragraphs that have been removed.

Engagement with the Professional Bodies

Technical Staff received feedback from the professional bodies on the Proposed June 2021 ED. Technical Staff provided written feedback to, and met on 26 August 2021 with, the professional bodies concerning how the matters raised by them have been dealt with in Proposed APES 320 ED (Agenda Item 7(c)).

Technical Staff have addressed the vast majority of the matters raised by the professional bodies, and they are generally supportive of the changes made. However, some remaining matters are discussed below.

CA ANZ raised an issue whether APES 320 should be a 'Level 1' standard setting out a system of quality control/management regardless of the service, and ASQM 1 could be a 'Level 2' standard focused on those particular services. Technical Staff are concerned this approach would either require confirmation that compliance with ASQM 1 means APES 320 is complied with, or alternatively, assurance practices would have to demonstrate how they have complied with ASQM 1 and APES 320.

- 1) *Technical Staff propose to include a Request for Specific Comment in the APES 320 Exposure Draft to obtain broad stakeholder views on whether APES 320 should cover Non-Assurance Services only or all services.*

CPA Australia believe APES 320 should include root cause analysis as best practice for investigating NOCLAR or complaints and issues within the firm and that the Professional Standards Authority promotes the use of root cause analysis.

Technical Staff believe root cause analysis would add a significant level of complexity to the standard and may be more relevant to assurance practices. The IAASB included root cause analysis in ISQM 1 relating to quality for assurance engagements in paragraphs 41-43, 58, A158, A161, A163-173, A181, A186 and A192-A193, consisting of approximately 5 ½ pages of requirements and application material.

The Professional Standards Council encourages the use of root cause analysis for associations regarding adverse events that are chronic, recurring and possibly systemic.¹ Technical Staff note root cause analysis may be relevant in determining systemic issues but may be too complex and resource-intensive for SMPs and sole practitioners to implement.

- 2) *Technical Staff propose to include a Request for Specific Comment in the APES 320 Exposure Draft to obtain broad stakeholder views on whether APES 320 should include root cause analysis.*

IPA believe the standard should address the implications for hybrid firms to assist with implementation. CPA Australia suggested a mapping of APES 320 to ASQM 1 to assist hybrid firms. To address these concerns, Technical Staff have improved the flowchart in Appendix 1 to demonstrate which standards apply to firms and developed a new proposed Appendix 2 to demonstrate the high-level alignment between proposed APES 320 and ASQM 1 with paragraph references for all elements and components of the standards.

Large National Networks (LNN) Discussion Group

Technical Staff presented at the LNN meetings on 28 July 2021 (on APES 320's status and an updated mapping table at that date) and 25 August 2021 (on the Proposed APES 320 ED – Agenda Item 7(c)). The following matters were discussed:

- Experienced mid-tier practitioners believe there is nothing broken with extant APES 320, no burning platform for change and support using extant APES 320 material where possible.
- Mid-tier firms noted that the alignment between APES 320 and ASQM 1 was positive, will make it much easier for hybrid firms and provides a clear path and clarity.

¹ [Professional Standards Council Annual Report 2019-20](#).

- Assurance practices will be the main focus to implement ASQM 1, highlighting the importance of aligning APES 320 and ASQM 1 and implementing changes simultaneously, especially for SMP hybrid firms with fewer resources.
- A Big six firm representative's view was that with the focus on audit practices and ASQM 1, a longer implementation time for APES 320 could be beneficial and use learnings from ASQM 1's implementation.
- The critical importance of releasing an APES 320 ED as soon as possible to enable firms to commence implementation, professional bodies to develop tools and guidance, and AUASB and APESB to continue collaborating and assisting firms in dealing with changes required for both standards at the same time.
- Different views were expressed on the level of compliance with the existing APES 320 concerning non-assurance services. It was noted that professional bodies had reported increases in compliance levels 70-80%, and the proposed changes provide an opportunity to educate and further increase compliance levels.
- A professional body representative believed Option 2 to create a new quality management standard for non-assurance services could be beneficial. However, this was not supported by experienced practitioners due to the significant impact for hybrid firms.
- That root cause analysis (such as in ASQM 1) is more relevant to assurance engagements and may be too onerous for non-assurance services.
- The combination of APES 320 and APES 325 is impacted by APES 325 applying to the entire firm, whereas APES 320 will only cover non-assurance practices.

Changing the name of APES 320

Technical Staff believe changing the name of APES 320 to *Quality Management for Firms that perform Non-Assurance Services* would make it more transparent as to what aspects of firms are covered by the standard at the outset, and the naming convention is consistent with ASQM 1.

Technical Staff recommend that the Board approve changing the name of the standard to APES 320 Quality Management for Firms that perform Non-Assurance Services.

References to and relevance of APES 320

Agenda Item 7(e) lists entities that refer to APES 320 or where APES 320 is relevant to such entities and APESB pronouncements that include references to APES 320. This research demonstrates numerous entities place weight on APES 320's quality requirements, and removing certain requirements or establishing a new system could have unintended consequences and reduced reliance on this standard.

Further, it demonstrates the importance of having appropriate quality policies and procedures when providing non-assurance services, including forensic accounting, taxation, valuation and insolvency services, compilations or engagements relating to public documents to ensure professional standards, legal and regulatory requirements are complied with and reports issued are appropriate.

APES 325 Risk Management for Firms

In Technical Staff's discussions with the professional bodies, they have raised whether APES 320 and APES 325 could be combined as the system of quality control/management is embedded in the risk management of a firm.

Agenda Item 7(a) explores the pros and cons of consolidating APES 320 and APES 325. The Proposed APES 320 ED (Agenda Item 7(c)) removes the requirements for assurance engagements and assurance concepts, addresses non-assurance services and can no longer be considered a standard addressing assurance and non-assurance services. Whereas APES 325 covers both assurance and non-assurance practices.

APES 325 is intended to be used by those responsible for the firm's governance, while APES 320 is designed to be used by those who undertake engagements and are accountable for engagement quality. Combining the standards risks losing focus on broader firm governance matters, including facilitating business continuity and protecting firms' reputations and credibility.

Technical Staff believe that combining the standards would cause unnecessary disruption requiring all firms to re-establish their risk management frameworks in the current environment. Accordingly, Technical Staff believe on balance that this option should not be adopted.

Proposed paragraph 3.4 of APES 320 illustrates the linkage between APES 320 and APES 325, noting the policies and procedures required for APES 320 are to be embedded within the risk management framework required under APES 325. This is also enhanced by changing references in APES 320 from Reasonable Assurance to reasonable confidence, being terminology used in APES 325.

- 3) *Technical Staff propose to include a Request for Specific Comment in the APES 320 Exposure Draft to obtain broad stakeholder views on whether APES 320 and APES 325 should remain as separate standards or be consolidated into one standard.*

Technical Staff note that if the proposals for APES 320 are adopted, consequential amendments to APES 325 will be required. In particular, [paragraph 3.3](#) of APES 325 will need to be considered to encapsulate quality management systems under ASQM 1 being embedded within the risk management framework.

Impact on SMPs

Technical Staff have considered the impact of the proposed changes to APES 320 on SMPs and believe Option 1 will have the lowest impact as it:

- creates the least disruption;
 - enables SMPs to maintain existing policies and procedures with minimal changes;
 - provides high-level alignment to ASQM 1 and enables changes to occur over the same period to reduce resource implications for SMP hybrid firms.
- 4) *Technical Staff propose to include a Request for Specific Comment in the APES 320 Exposure Draft on whether the development of additional implementation material would be useful for SMPs.*

Way Forward

Subject to the Board's views and direction, Technical Staff propose the following way forward:

1. seek the Board's views, direction and review comments on the Proposed Exposure Draft for APES 320 ED 05/21 (Agenda Item 7(c));
2. issue an Exposure Draft for APES 320 ED 05/21 by mid to late September 2021 requesting public comments over 60 days ending late November 2021;
3. seek approval from the Board to issue the revised APES 320 at 1st Board meeting of 2022;

4. release the revised APES 320 by February 2022 (with an effective date of 1 January 2023), allowing approximately 11 months for implementation with early adoption permitted; and
5. consider consequential amendments to APES 325 resulting from changes to APES 320.

Staff Recommendation

The Board:

- note Technical Staff's assessment of options for APES 320 and APES 325;
- approve:
 - subject to the Board's review comments and editorials, the issue of an Exposure Draft on proposed revisions to APES 320 (ED 05/21);
 - changing the name of APES 320 to *Quality Management for Firms that provide Non-Assurance Services*; and
 - Technical Staff's proposed way forward for APES 320 and APES 325.

Materials Presented

Agenda Item 7(a)	Analysis of Options for APES 320 and APES 325
Agenda Item 7(b)	Summary of changes made to APES 320 ED
Agenda Item 7(c)	Proposed Exposure Draft APES 320 ED 05/21
Agenda Item 7(d)	Table mapping proposed APES 320 to extant APES 320
Agenda Item 7(e)	References to and relevance of APES 320

Authors: Channa Wijesinghe
Jon Reid

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