

Agenda Item 3-D



International Auditing
and Assurance
Standards Board

Introduction

The International Auditing and Assurance Standards Board (IAASB) issued *A Framework for Audit Quality: A Discussion of Key Elements that Create an Environment for Audit Quality* (“Framework”) in xxxxx, 2014. The Framework describes key attributes that are conducive to audit quality, reflecting the different perspectives of stakeholders. It outlines the Inputs, Outputs, Interactions, and Contextual Factors that create an environment within an audit firm and a jurisdiction which maximizes the likelihood that quality audits are performed on a consistent basis.

The Inputs are listed in the Framework at the engagement, firm, and national levels, but are not described in detail. The purpose of this Guide—*A Guide to Input Factors*—is to provide additional detail on the inputs to assist users of the Framework.

This Guide includes a section describing the Framework so that users of the Guide are provided with the appropriate context within which the detailed descriptions of the Inputs can be read. However, it should be read in conjunction with the full Framework, which can be downloaded from the IAASB website (www.iaasb.org).

Neither the Framework nor the Guide is a substitute for relevant auditing standards and standards of quality control within audit firms, as well as ethics and other regulatory requirements. Additionally, they do not establish additional standards or provide procedural requirements for the performance of audit engagements.

The IAASB Framework for Audit Quality

1. Auditors are responsible for the quality of ~~individual the financial statement audits they perform, and should aim to ensure that quality audits are consistently performed.~~ **A quality audit** is likely to be achieved when the auditor's opinion on the financial statements ~~can be relied upon as it was~~ based on sufficient appropriate audit evidence about whether material misstatements exist, obtained by an engagement team that:

- Exhibited appropriate values, ethics and attitudes;
- Was sufficiently knowledgeable, skilled, and experienced and had sufficient time allocated to perform the audit work;
- Applied a rigorous audit process and quality control procedures that complied with law, regulation and applicable standards;
- Provided ~~valuable~~ useful and timely reports; and
- Interacted appropriately with ~~a variety of different~~ relevant stakeholders.

2. The concept of **audit quality** captures the key elements that create an environment within an audit firm and a jurisdiction which maximizes the likelihood that quality audits are performed on a consistent basis. Audit quality is influenced by the firm level and national level attributes described in this Framework. ~~Many factors contribute to enhancing audit quality within a jurisdiction, and increasing the likelihood of quality audits being consistently performed.~~

3. The IAASB believes there is value in describing ~~these~~ factors relating to both a quality audit and audit quality and thereby encouraging auditors, audit firms and other stakeholders to challenge themselves about whether there is more they can do to increase audit quality in their particular environments.

2. The Framework described in this paper sets out the key attributes that are conducive to audit quality, reflecting the different perspectives of stakeholders. The objectives of the Framework include:

- Raising awareness of the key elements of audit quality;
- Encouraging key stakeholders to explore ways to improve audit quality; and
- Facilitating greater dialogue between key stakeholders on the topic.

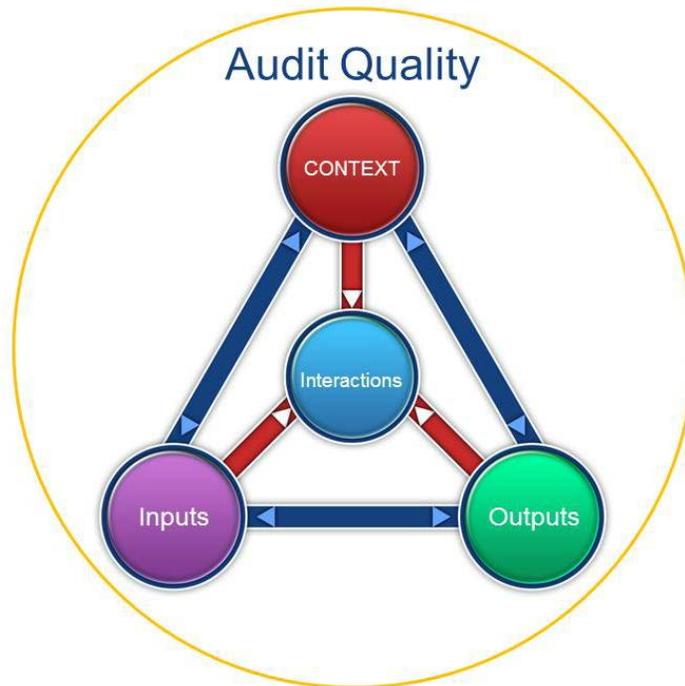
4. The Framework applies to audits of all entities regardless of their size, nature, and complexity. It also applies to and all audit firms regardless of size, including audit firms that are part of a network or association. However, the attributes can vary in importance and affect audit quality in subtly different ways. In particular, public sector auditors (due to their societal role and constitutional mandate) and auditors of smaller entities may give specific emphasis to certain factors.

3-5. Auditors are required to comply with relevant auditing standards and standards of quality control within audit firms, as well as ethics and other regulatory requirements. The Framework is not a substitute for such standards, nor does it establish additional standards or provide procedural requirements for the performance of audit engagements.

- ~~The Framework applies to both private sector and public sector audits although, due to their societal role and constitutional mandate, public sector audit bodies may give specific emphasis to certain factors; and~~
 - ~~Aspects of the Framework may have specific impacts on the audits of smaller entities.~~
- ~~Section 5 of the Framework, *Considerations Relating to Specific Audits*, provides additional commentary.~~

4.6. While the quality of an individual audit will be influenced by the inputs, outputs and interactions described in this Framework, the Audit Quality Framework, by itself, will not be sufficient for the purpose of evaluating the quality of an individual audit. This is because detailed consideration will need to be given to matters such as the nature and extent of audit evidence obtained in response to the risks of material misstatement in a particular entity, the appropriateness of the relevant audit judgments made, and compliance with relevant standards.

5.7. The Framework distinguishes the following elements:



Inputs

6.8. Inputs are grouped into the following categories:

- (a) The values, ethics and attitudes of auditors, which in turn, are influenced by the culture prevailing within the audit firm;

- (b) The knowledge, skills, and experience of auditors and the time allocated for them to perform the audit; and
- (c) The effectiveness of the audit process and quality control procedures.

~~7-9.~~ Within these categories, quality attributes are further organized between those that apply directly at:

- (a) The audit engagement level;
- (b) The level of an audit firm, and therefore indirectly to all audits undertaken by that audit firm; and
- (c) The national (or jurisdictional) level and therefore indirectly to all audit firms operating in that country and the audits they undertake.

~~8-10.~~ The inputs to audit quality will be influenced by the context in which an audit is performed, the interactions with key stakeholders and the outputs. For example, law and regulations (context) may require specific reports (output) that influence the skills (input) utilized.

Outputs

~~11.~~ Outputs include reports and information that are formally prepared and presented by one party to another, as well as outputs that arise from the auditing process that are generally not visible to those outside the audited organization. For example, these may include improvements to the entity's financial reporting practices and internal control over financial reporting, that may result from auditor observations.

~~9-12.~~ Outputs—The outputs from the audit are often determined by the context, including legislative requirements. While some stakeholders can influence the nature of the outputs, others have less influence. Indeed, for some stakeholders, such as investors in listed companies, the auditor's report is the primary output and ~~currently this is relatively standardized.~~

Interactions Among Key Stakeholders

~~4-13.~~ While each separate stakeholder in the financial reporting supply chain plays an important role in supporting high-quality financial reporting, the way in which the stakeholders interact can have a particular impact on audit quality. These interactions, including both formal and informal communications, will be influenced by the context in which the audit is performed and allow a dynamic relationship to exist between inputs and outputs. For example, discussions between the auditor and ~~those charged with governance~~ the audit committee of a listed company at the planning stage can influence the use of specialist skills (input) and the form and content of the auditor's report to those charged with governance (output). In contrast, for privately owned businesses, there may be close proximity to the owners during the course of the audit. In these circumstances, there may be frequent informal communications, which contribute to audit quality.

Context

~~14.~~ There are a number of contextual factors that can facilitate financial reporting quality, including corporate governance and the applicable financial reporting framework. ~~These contextual factors, including legislative and regulatory requirements, also help shape the interactions Among among key stakeholders, as well as the arrangements within the audited entity and the audit firm. These factors~~ They can also impact ~~audit~~ the risk of material misstatements in the financial statements

~~and, the nature and extent of audit evidence required, and the efficiency of the audit process. Where appropriate, auditors need to respond to these issues when determining what constitutes sufficient appropriate audit evidence, and this may have an impact on the efficiency of the audit process.~~

~~44-15. There are also contextual factors that relate more directly to audit quality, including regulation and the financial reporting timetable.~~

~~42.~~

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Summary of Attributes

~~43-16.~~ The IAASB's Framework contains the following attributes. The numbering of each of these inputs, outputs, and contextual factors in the following table corresponds to the section and subsection number on the following pages.

Framework Element	Attributes
1. INPUTS INPUTS – Values, Ethics, and Attitudes	<p>1.1 Engagement Level</p> <p>1.1.1 The engagement team recognizes; that the audit is performed in the wider public interest <u>and the importance of complying with ethical requirements.</u></p> <p>1.1.2 The engagement team exhibits objectivity and integrity.</p> <p>1.1.3 The engagement team is independent.</p> <p>1.1.4 The engagement team exhibits professional competence and due care.</p> <p>1.1.5 The engagement team exhibits professional skepticism.</p> <p>1.2 Firm Level</p> <p>1.2.1 Governance arrangements are in place that establish independence <u>and the appropriate "tone at the top." And which recognize and promote the importance of independence.</u></p> <p>1.2.2 The firm promotes the personal characteristics <u>has appropriate appraisal and reward systems</u> essential to audit quality.</p> <p>1.2.3 Financial considerations do not drive actions and decisions that may have a negative effect on <u>reduce audit quality to an unacceptable level.</u></p> <p>1.2.4 The firm emphasizes the importance of providing partners and staff <u>with continuing professional development opportunities and access</u> to high-quality technical support.</p> <p>1.2.5 The firm promotes a culture of consultation on difficult issues.</p> <p>1.2.6 Robust systems exist for making client acceptance and continuance decisions.</p> <p>1.3 National Level</p> <p>1.3.1 Ethics requirements are promulgated that make clear both the underlying ethics principles and the specific requirements that apply.</p> <p>1.3.2 Regulators and professional accountancy organizations are active in ensuring that the ethics principles are understood and the requirements</p>

Framework Element	Attributes
	<p>are consistently applied.</p> <p>1.3.3 Information relevant to client acceptance decisions is shared between audit firms.</p>
<p>INPUTS – Knowledge, Experience and Time</p>	<p>1.4 Engagement Level</p> <p>1.4.1 Partners and staff have the necessary competences.</p> <p>1.4.2 Partners and staff understand the entity's business.</p> <p>1.4.3 Partners and staff make reasonable judgments.</p> <p>1.4.4 The audit engagement partner is actively involved in risk assessment, planning, supervising, and reviewing the work performed.</p> <p>1.4.5 Staff performing detailed "on-site" audit work have sufficient experience, their work is appropriately directed, supervised and reviewed, and there is a reasonable degree of staff continuity.</p> <p>1.4.6 Partners and staff have sufficient time to undertake the audit in an effective manner.</p> <p>1.4.7 The audit engagement partner and other experienced members of the audit team are accessible to management and those charged with governance.</p> <p>1.5 Firm Level</p> <p>1.5.1 Partners and staff have sufficient time to deal with difficult issues as they arise.</p> <p>1.5.2 Engagement teams are properly structured.</p> <p>1.5.3 Partners and more senior staff provide less experienced staff with timely appraisals and appropriate coaching or "on-the-job" training.</p> <p>1.5.4 Sufficient training is given to audit partners and staff on audit, accounting and, where appropriate, specialized industry issues.</p> <p>1.6 National Level</p> <p>1.6.1 Robust arrangements exist for licensing audit firms/individual auditors.</p> <p>1.6.2 Education requirements are clearly defined and training is adequately resourced <u>and effective</u>.</p> <p>1.6.3 Arrangements exist for briefing auditors on current issues and for providing training to them in new accounting, auditing or regulatory requirements.</p> <p>1.6.4 The auditing profession is well-positioned to attract and retain high-quality individuals.</p>
<p>INPUTS – Audit Process and Quality Control Procedures</p>	<p>1.7 Engagement Level</p> <p>1.7.1 The engagement team complies with auditing standards, relevant laws and regulations, and the audit firm's quality control procedures.</p> <p>1.7.2 The engagement team makes appropriate use of information technology.</p> <p>1.7.3 There is effective interaction with others involved in the audit including, where applicable, internal auditors.</p>

Framework Element	Attributes																
	<p>1.7.4 There are appropriate arrangements with management so as to achieve audit efficiency.</p> <p>1.7.5 There is appropriate audit documentation.</p> <p>1.8 Firm Level</p> <p>1.8.1 The audit methodology is adapted to developments in professional standards and to findings from internal quality control reviews and external inspections.</p> <p>1.8.2 The audit methodology encourages individual team members to apply professional skepticism and exercise appropriate professional judgment.</p> <p>1.8.3 The methodology requires effective supervision and review of audit work.</p> <p>1.8.4 The methodology requires appropriate audit documentation.</p> <p>1.8.5 Rigorous quality control procedures are established and audit quality is monitored and appropriate consequential action is taken.</p> <p>1.8.6 Where required, effective engagement quality control reviews are undertaken.</p> <p>1.9 National Level</p> <p>1.9.1 Auditing <u>and other</u> standards are promulgated that make clear the underlying objectives as well as the specific requirements that apply.</p> <p>1.9.2 Bodies responsible for external audit inspections consider relevant attributes of audit quality, both within audit firms and on individual audit engagements.</p> <p>1.9.3 Effective systems exist for investigating allegations of audit failure and taking disciplinary action when appropriate.</p>																
Framework Element	Attributes																
2. OUTPUTS	<p>The value and timeliness of:</p> <table border="1" data-bbox="386 1318 1166 1692"> <thead> <tr> <th data-bbox="386 1318 683 1360">2.1 Engagement Level</th> <th data-bbox="683 1318 1166 1360">From the Auditors</th> </tr> </thead> <tbody> <tr> <td data-bbox="386 1360 683 1423"></td> <td data-bbox="683 1360 1166 1423">2.1.1 Auditor's reports to users of audited financial statements</td> </tr> <tr> <td data-bbox="386 1423 683 1486"></td> <td data-bbox="683 1423 1166 1486">2.1.2 Auditor's reports to those charged with governance</td> </tr> <tr> <td data-bbox="386 1486 683 1528"></td> <td data-bbox="683 1486 1166 1528">2.1.3 Auditor's reports to management</td> </tr> <tr> <td data-bbox="386 1528 683 1591"></td> <td data-bbox="683 1528 1166 1591">2.1.4 Auditor's reports to financial and prudential regulators</td> </tr> <tr> <td data-bbox="386 1591 683 1633"></td> <td data-bbox="683 1591 1166 1633">From the Entity</td> </tr> <tr> <td data-bbox="386 1633 683 1675"></td> <td data-bbox="683 1633 1166 1675">2.1.5 The audited financial statements</td> </tr> <tr> <td data-bbox="386 1675 683 1692"></td> <td data-bbox="683 1675 1166 1692">2.1.6 Reports from those charged with</td> </tr> </tbody> </table>	2.1 Engagement Level	From the Auditors		2.1.1 Auditor's reports to users of audited financial statements		2.1.2 Auditor's reports to those charged with governance		2.1.3 Auditor's reports to management		2.1.4 Auditor's reports to financial and prudential regulators		From the Entity		2.1.5 The audited financial statements		2.1.6 Reports from those charged with
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Framework Element	Attributes	
		<p>governance, including audit committees</p> <p>From Audit Regulators</p> <p>2.1.7 Providing information on individual audits</p>
	<p>2.2 Firm and National Levels</p>	<p>From the Audit Firm</p> <p>2.2.1 Transparency reports</p> <p>2.2.2 Annual <u>and other</u> reports</p> <p>From Audit Regulators</p> <p>2.2.3 Providing an aggregate view on the results of audit firm inspections</p>
<p>3. INTERACTIONS</p>	<p>Effective Interactions Between:</p> <p>Auditors and management, those charged with governance, users, regulators</p> <p>Management and those charged with governance, regulators, users</p> <p>Those charged with governance and regulators, users</p> <p>Regulators and users</p>	
<p>4. CONTEXTUAL FACTORS</p>	<p><u>Financial Reporting Quality</u></p> <p>4.1.1 Business practices and commercial law</p> <p>4.1.2 Laws and regulations relating to financial reporting</p> <p>4.1.3 The applicable financial reporting framework</p> <p>4.1.4 Corporate governance</p> <p>4.1.5 Information systems</p> <p>4.1.6 Financial reporting timetable</p> <p>4.1.7 1.6 Broader cultural factors</p> <p><u>Audit Quality</u></p> <p>4.2.1 Corporate governance</p> <p>4.2.2 Regulation</p> <p>4.2.3 Litigation Environment</p> <p>4.2.4 Education and Talent</p> <p>4.2.5 Financial Reporting Timetable</p> <p>4.1.8</p>	

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1. Input Factors

44.17. Quality audits involve auditors:

- Exhibiting appropriate values, ethics and attitudes;
- Being sufficiently knowledgeable, skilled, and experienced and having ~~adequate~~ sufficient time allocated to them to ~~undertake~~ perform the audit their work; and
- Applying a rigorous audit process and quality control procedures that comply with law, regulation and applicable standards.

45.18. Key attributes that foster audit quality are described below. These attributes apply at the audit engagement level, at the audit firm level, and at a national (or jurisdictional)¹ level. Each attribute and level is described in separate sections.

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
Knowledge, Experience, and Time	Section 1.4	Section 1.5	Section 1.6
Audit Process and Quality Control Procedures	Section 1.7	Section 1.8	Section 1.9

1.1. Values, Ethics and Attitudes – Engagement Level

46.19. The audit engagement partner² is responsible for an audit engagement and therefore directly responsible for audit quality. In addition to taking responsibility for the performance of the audit, the audit engagement partner has a critical role in ensuring that the engagement team exhibits the values, ethics and attitudes necessary to support a quality audit, including skepticism. Key attributes are:

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
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Audit Process and Quality Control Procedures	Section 1.7	Section 1.8	Section 1.9

¹ A jurisdiction can be larger or smaller than a country. In some areas of the world some aspects of audit regulation span a number of countries. In some countries aspects of audit regulation are undertaken by smaller units such as states or provinces.

² In the public sector environment, the terms "client," "engagement," "engagement partner," and "firm" should, where relevant, be read as referring to their public sector equivalents as defined in International Standard of Supreme Audit Institutions (ISSAI) 40, Quality Control for Supreme Audit Institutions, Section 7.

- The engagement team recognizes; that the audit is performed in the wider public interest; and the importance of complying with ethical requirements.³
- The engagement team exhibits objectivity and integrity.
- The engagement team is independent.
- The engagement team exhibits professional competence and due care.
- The engagement team exhibits professional skepticism.

1.1.1. *The Engagement Team Recognizes; that the Audit Is Performed in the Wider Public Interest; and the Importance of Complying with Ethical Requirements*

~~17-20.~~ The audit team needs to be committed to performing the audit in the interests of the entity's stakeholders and in the wider public interest. The nature and extent of the public interest is likely to vary according to the nature of the entity. For this reason However, in all audits the audit team needs to provide an appropriate degree of challenge to management, robustly express their views, and pursue matters to appropriate conclusions, and make appropriate judgments

1.1.2. *The Engagement Team Exhibits Objectivity and Integrity*

~~18-21.~~ The principle of objectivity imposes an obligation on auditors not to compromise their professional or business judgment because of bias, conflict of interest or the undue influence of others.⁴

~~19-22.~~ The need for auditors, in particular, to be objective arises from the fact that many of the important issues involved in the preparation of financial statements involve judgment. Few items included in the financial statements can be measured with certainty, and many involve estimation and therefore judgment. Auditors need to be objective when they evaluate management judgments to reduce the risk that the financial statements are materially misstated by through management bias, whether deliberately or inadvertently, making a biased judgment or following an otherwise inappropriate accounting practice.

~~20-23.~~ Integrity is a prerequisite for all those who act in the public interest. It is essential that the engagement team acts, and is seen to act, with integrity, which requires not only honesty but a broad range of related qualities such as fairness, candor, and courage.

1.1.3. *The Engagement Team Is Independent*

~~24-24.~~ Independence is required to safeguard individual members of the engagement team or the audit firm from influences that may compromise professional judgments, thereby and helps allowing them to act with integrity, and exercise objectivity (independence of mind) and professional skepticism. It is also required to avoid facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude that a firm's, or a member of the

³ The IESBA *Code of Ethics for Professional Accountants* identifies five fundamental principles of professional ethics for professional accountants: integrity, objectivity, professional competence and due care, confidentiality, and professional behavior.

⁴ The International Ethics Standards Board for Accountants *Code of Ethics for Professional Accountants* (IESBA Code), paragraph 120.1

audit team's, integrity, objectivity (independence in appearance) or professional skepticism has been compromised.

~~22-25.~~ Threats to auditor independence may include:

- Financial interests existing between the auditor and the audited entity. Holding a financial interest in an audit client may create a self-interest threat.
- Business relationships between the auditor and the audited entity. A close business relationship between the audit firm, or a member of the engagement team or an immediate family member, and the entity may create self-interest or intimidation threats.
- Provision of non-audit services to audit clients. Audit firms have traditionally provided to their audit clients a range of non-audit services that are consistent with their skills and expertise. Providing non-audit services may, however, create threats to independence. The threats created are most often self-review, self-interest and advocacy threats.
- Partners and staff may believe that their remuneration and, indeed, their ongoing careers with the audit firm are dependent on retaining an audit client, creating a familiarity or self-interest threat.
- Situations where a former member of the audit team, or partner of the firm, has joined the audited entity in a position to exert significant influence over the preparation of the accounting records and financial statements. The threats created are most often familiarity, self-interest and intimidation threats.

~~23-26.~~ A familiarity threat may also be created by using the same senior personnel on an audit engagement over a long period of time. However, accumulated prior knowledge of the entity and its business is likely to be conducive to audit quality as it will enhance the auditor's assessment of, and responses to, risks; as well as lead to efficiency and the most insightful recommendations for improvement in particular areas of an entity's business operations.

27. Threats to auditor independence need to be balanced with the potential benefits to audit quality that arise from the senior personnel's detailed knowledge of the entity and its business resulting from involvement in the audit over a number of years. To address this threat, the IESBA Code requires key audit partners of public interest entities to change (or "rotate") after seven years; ethics or legal requirements in some countries mandate a shorter rotation period. Some believe that in addition to the rotation of audit engagement partners, auditor independence would be strengthened if the audit firm itself were to be periodically changed. Others believe that retaining the same firm is likely to assist the auditors in understanding the entity's business and systems and result in effective responses to business-risks of material misstatement in the financial statements, as well as audit efficiency.

28. The consideration of threats and safeguards when determining independence for public sector audits is as important as for audits in the private sector. However, some of the potential threats may differ. For example, it is less likely that auditors in the public sector will have direct financial interests in the entities they audit.

~~24-29.~~ The auditor is often viewed as a valued business and tax advisor to the entity and there are usually frequent direct communications with senior management, resulting in the auditor being well informed about business developments. This gives the auditor good knowledge of both the client's

financial reporting process and its industry, but can also be seen as a threat to independence. Smaller entities will often plan to utilize the auditor's financial reporting expertise in assisting with the preparation and presentation of annual financial statements. Where this involvement is permitted, it can assist the auditor with understanding the entity and its accounting systems but could result in threats to auditor objectivity that need to be mitigated by safeguards. In some jurisdictions the auditor is prevented from providing accounting assistance.

1.1.4. *The Engagement Team Exhibits Professional Competence and Due Care*

~~25-30.~~ Professional competence and due care involves all members of the engagement team:

- ~~Developing and m~~Maintaining professional knowledge and skill at an appropriate level;
- Acting carefully, thoroughly and on a timely basis; and
- Acting diligently in accordance with applicable technical and professional standards.

1.1.5. *The Engagement Team Exhibits Professional Skepticism*

~~26-31.~~ Professional skepticism is an attitude that includes the application of a questioning mindset in the context of an appropriate understanding of the entity, its business and the environment in which it operates. This understanding, together with more general business knowledge and experience, allows the auditor to assess the risks of material misstatement in an entity's financial statements, assess the adequacy of audit evidence, and reach appropriate conclusions.

~~27-32.~~ Professional skepticism is an important aspect of auditor judgment related to planning, performing and evaluating the results of an audit. Unless auditors are prepared to challenge management's assertions, they will not act as a deterrent to fraud nor be able to conclude, with confidence, ~~that whether~~ an entity's financial statements are fairly presented in accordance with the financial reporting framework.

~~28-33.~~ Professional skepticism involves all members of the engagement team:

- ~~Having-having~~ a questioning mind and a willingness to challenge management assertions;
- ~~Assessing-assessing~~ critically the information and explanations obtained in the course of their work;
- ~~Seeking-seeking~~ to understand management motivations for possible misstatement of the financial statements;
- ~~Keeping-keeping~~ an open mind;
- challenging the judgments of other members of the engagement team;
- ~~Having-having~~ the confidence to challenge management and the persistence to follow things through to a conclusion; and
- ~~Being-being~~ alert for evidence that is inconsistent with other evidence obtained or calls into question the reliability of documents and responses to inquiries.

1.2. Values, Ethics and Attitudes – Firm Level

~~29-34.~~ The audit firm's culture has an important influence on the values, ethics and attitudes of audit partners and other members of the engagement team because the environment in which the engagement team works can materially affect the mindset of partners and staff, and consequently the way they discharge their responsibilities. While the audit is designed to protect the public interest, audit firms are often commercial entities. Each firm's culture will be an important factor in determining ~~the extent to which~~ how its partners and staff function in the public interest ~~as opposed to merely achieving~~ and how this is satisfactorily aligned with the firm's commercial goals.

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
Knowledge, Experience, and Time	Section 1.4	Section 1.5	Section 1.6
Audit Process and Quality Control Procedures	Section 1.7	Section 1.8	Section 1.9

~~30-35.~~ Key attributes in relation to creating a culture where audit quality is valued are:

- Governance arrangements are in place that establish ~~independence and~~ the appropriate "tone at the top", and which ~~recognize and promote the importance of independence.~~
- The firm has appropriate appraisal and reward systems ~~promotes the personal characteristics~~ essential to audit quality.
- Financial considerations do not drive actions and decisions that may ~~have a negative effect~~ or reduce audit quality to an unacceptable level.
- The firm emphasizes the importance of providing partners and staff with continuing professional development opportunities and access to high-quality technical support.
- The firm promotes a culture of consultation on difficult issues.
- Robust systems exist for making client acceptance and continuance decisions.

1.2.1 *Governance Arrangements Are in Place that Establish ~~Independence and~~ the Appropriate "Tone at the Top", and which Recognize and Promote the Importance of Independence*

~~34-36.~~ The firm's leadership has a vital role in avoiding situations that might compromise the firm's objectivity or independence. Creating an appropriate environment within the audit firm includes encouraging adherence to the principles underlying ethics requirements that apply to auditors.

37. It is also important that an audit firm has robust internal governance arrangements to safeguard the public interest nature of the audit function and to avoid the firm's commercial interests adversely affecting audit quality, for example, by inappropriately promoting other practice areas (such as tax, corporate finance and consultancy) to the detriment of audit quality.

~~32-38.~~ Sole practitioners have direct control over their firm's culture, and in Small and Medium-Practices (SMPs) a small number of partners can have a very direct influence over input factors such as governance arrangements, consultation, and monitoring activities. Depending on the tone, this could be either a strength, or a weakness, of the small firm environment.

1.2.2 *The Firm Promotes the Personal Characteristics that are Appropriate Appraisal and Reward Systems Essential to Audit Quality*

~~39. It is also important that partners and staff are periodically appraised on the basis of audit quality, using appropriate competency frameworks, and that conclusions are used to support promotion and remuneration decisions.~~ Appraisal and reward systems need to nurture and develop appropriate personal characteristics and behavior, including integrity, objectivity, professional competence and due care, need to be nurtured and developed by the firm. This involves embedding these characteristics in recruitment selection criteria and in training programs, using appropriate competency frameworks. ~~It is also important that partners and staff are periodically appraised on the basis of audit quality, using appropriate competency frameworks, and that conclusions are used to support promotion and remuneration decisions.~~

40. Competence frameworks might best be developed by reference to the competence areas of the International Education Standards (IESs), which would promote harmonization of the frameworks among audit firms.

~~33-41.~~ Conclusions reached are used to support promotion and remuneration decisions; as well as other actions that may be taken by firms when partners' or staff performance has not met expected standards. Audit firms also need to ensure that audit partners and staff are not penalized for jeopardizing a client relationship by taking a robust position on audit issues.

~~34.~~ Audit firms also need to ensure that audit partners and staff are not penalized for jeopardizing a client relationship by taking a robust position on audit issues.

1.2.3 *Financial Considerations Do Not Drive Actions and Decisions that May Have a Negative Effect on Reduce Audit Quality to an Unacceptable Level*

~~35-42.~~ Financial considerations both at the firm level (such as the financial target that a firm sets for the profit margin to be achieved on audit work and the willingness to invest in training and support systems for audit) and at the engagement level (such as the relationship between the audit fee and the underlying cost of the work performed) should not be allowed to prevent the performance of a robust audit that meets the public interest.

~~36-43.~~ There should also not be, at the expense of audit quality:

- Emphasis on winning audit appointments and on the retention of audit clients, particularly at unrealistically low fees, ~~at the expense of audit quality;~~
- Emphasis on marketing non-audit services to entities that the firm audits ~~at the expense of undertaking a quality audit; or~~
- Cost cutting (including by reducing partners and staff) in the audit practice (for example, during times of economic downturn) ~~to the detriment of audit quality.~~

1.2.4 *The Firm Emphasizes the Importance of Providing Partners and Staff with Continuing Professional Development Opportunities and Access to High-Quality Technical Support*

~~37-44.~~ Auditing requires knowledge of a considerable number of technical areas including financial reporting, auditing and ethics standards, and corporate and tax laws and regulations. It is important

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that audit firms have technical support arrangements to help individual partners and staff keep up to date with developments in these areas and to provide assistance on complex areas.

45. Audit quality can also be enhanced if an information infrastructure is developed that enables the firm to support audit judgments (for example, by assembling business and industry-related databases), to track and appropriately address independence issues, and to plan and effectively manage the rotation of partners on audit engagements.

46. The size of audit firms and the technical support available can vary considerably. For smaller practices with a small number of staff and a client base with relatively little complexity in operations, it is possible to develop relatively straightforward quality control policies and procedures. However, smaller practices can face challenges in relation to consultation and may need to employ external consultants to provide technical expertise when needed or may rely on technical support services provided by local professional accounting organizations

1.2.5 The Firm Promotes a Culture of Consultation on Difficult Issues

47. A culture of consultation is important for all audit firms. Auditing often requires difficult decisions and judgments to be made. Staff will discuss these issues within the audit team and with the audit engagement partner. Audit engagement partners ~~will often wish~~ should be encouraged to discuss difficult decisions and judgments with other partners or with technical specialists and give careful consideration of the advice given. For ~~t~~his process ~~will be facilitated if~~ to function effectively it is important that there is a culture of consultation and where those involved have sufficient time available to deal properly with issues as they arise.

~~38-48.~~ A culture of consultation is important for sole practitioners and SMPs, and in some cases, policies for engagement quality control reviews may be needed. While internal resources may be limited, external technical resources may be available to them, whether through their professional accountancy organizations, their relationships with other firms, or suitably resourced third-party organizations.

1.2.6 Robust Systems Exist for Making Client Acceptance and Continuance Decisions

~~39-49.~~ Prior to accepting an audit engagement, and annually thereafter, it is important that audit firms consider whether they are competent to perform the engagement and have the capabilities and resources to do so. This includes whether the firm can comply with relevant ethics requirements.

~~40-50.~~ While auditors need to be skeptical, ~~if an audit is to be undertaken cost effectively,~~ it also involves a degree of trust. Management lacking in integrity, by definition, cannot be trusted. Good client acceptance and continuance systems therefore evaluate whether there is information to suggest that client management lack integrity to the extent that it will not be possible to perform a quality audit. Having a rigorous client acceptance and continuance system is therefore important in helping an audit firm avoid engagements where there is a high chance of fraud or illegal acts, and thereby maintain a reputation for providing quality audits.

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1.3 Values, Ethics and Attitudes – National Level

44-51. National audit regulatory activities have an important influence on the culture within firms and the values, ethics and attitudes of audit partners and other members of the engagement team. Key attributes are:

- Ethics requirements are promulgated that make clear both the underlying ethics principles and the specific requirements that apply;
- Regulators and professional accountancy organizations are active in ensuring that the ethics principles are understood and the requirements are consistently applied; and
- Information relevant to client acceptance decisions is shared between audit firms.

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
Knowledge, Experience, and Time	Section 1.4	Section 1.5	Section 1.6
Audit Process and Quality Control Procedures	Section 1.7	Section 1.8	Section 1.9

1.3.1 *Ethics Requirements Are Promulgated that Make Clear Both the Underlying Ethics Principles and the Specific Requirements that Apply*

42-52. Ethics requirements may be imposed by law or regulations or mandated through professional accountancy organizations. The International Federation of Accountants (IFAC) requires its member bodies to take actions to adopt and implement the IESBA Code in their jurisdictions, and to assist in its implementation, depending on the member bodies' responsibilities in national environments. In some countries, the IESBA Code is supplemented by additional national requirements, and audit firms and public sector audit bodies may choose to impose higher requirements on their partners and staff.

43-53. Ethics requirements cannot address all possible situations. Therefore, auditors need to understand both the requirements and the fundamental principles underlying them and understand how to apply them in practice. An understanding of how to apply the principles can be developed through internal communications within the audit firm, through coaching or on-the-job training, and through staff observing more experienced staff in action.

44-54. The IESBA Code establishes, and requires auditors to comply with, the following fundamental principles of professional ethics:⁵

- Integrity – to be straightforward and honest in all professional and business relationships. Integrity also implies fair dealing and truthfulness.⁶
- Objectivity – to not allow bias, conflict of interest or undue influence of others to override professional or business judgments.
- Professional competence and due care – to maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent professional services based on current developments in practice, legislation and techniques, and act diligently and in accordance with applicable technical and professional standards.

⁵ IESBA Code, paragraph 100.5

⁶ IESBA Code, Section 110

- Confidentiality – to respect the confidentiality of information acquired as a result of professional and business relationships and, therefore, not disclose any such information to third parties without proper and specific authority, unless there is a legal or professional right or duty to disclose, nor use the information for the personal advantage of the professional accountant or third parties.
- Professional behavior – to comply with relevant laws and regulations, and avoid any action that discredits the profession.

~~45-55.~~ In addition, the IESBA Code contains additional requirements for auditor independence and describes the approach auditors should take, including:

- Identifying threats to independence;
- Evaluating the significance of the threats identified; and
- Applying safeguards, when necessary, to eliminate the threats or reduce them to an acceptable level.

~~46-56.~~ The IESBA Code states that when auditors determine that appropriate safeguards are not available or cannot be applied to eliminate the threats or reduce them to an acceptable level, the professional accountant shall eliminate the circumstance or relationship creating the threats or decline or terminate the audit engagement.⁷ In some situations, the IESBA Code recognizes that the threat created would be so significant that no safeguards could reduce the threat to an acceptable level; and accordingly an auditor is prohibited from undertaking the audit.

1.3.2 *Regulators and Professional Accountancy Organizations Are Active in Ensuring that the Ethics Principles Are Understood and the Requirements Are Consistently Applied*

~~47-57.~~ Consistent application of ethics requirements, and the principles that underlie them, is facilitated by guidance, training and support activities performed by regulators, professional accountancy organizations and others. This can include the issuance of guidance material such as answers to frequently asked questions as well as organizing interactive workshops.

1.3.3 *Information Relevant to Client Acceptance Decisions Is Shared between Audit Firms*

~~48-58.~~ Individual audit firms will make decisions on whether to accept a new, or continue with an existing, audit client. Firms may choose not to continue with an audit client if they have concerns about financial reporting practices or management integrity. In such circumstances, it is important that other audit firms who are invited to tender for the audit are aware of this information.

⁷ IESBA Code, paragraph 290.7. Public sector audit bodies are, however, not usually able to resign from audit engagements.

1.4 Knowledge, Experience and Time – Engagement Level

49-59. The audit engagement partner is responsible for being satisfied that the engagement team collectively has the appropriate competences and that the team has sufficient time to be able to obtain sufficient appropriate audit evidence before issuing the audit opinion.

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
Knowledge, Experience, and Time	Section 1.4	Section 1.5	Section 1.6
Audit Process and Quality Control Procedures	Section 1.7	Section 1.8	Section 1.9

50-60. Key attributes are:

- Partners and staff have the necessary competences.
- Partners and staff understand the entity's business.
- Partners and staff make reasonable judgments.
- The audit engagement partner is actively involved in risk assessment, planning, supervising, and reviewing the work performed.
- Staff performing detailed "on-site" audit work have sufficient experience, their work is appropriately directed, supervised and reviewed, and there is a reasonable degree of staff continuity.
- Partners and staff have sufficient time to undertake the audit in an effective manner.
- The audit engagement partner and other experienced members of the audit team are accessible to management and those charged with governance.

1.4.1 Partners and Staff Have the Necessary Competences

61. While not all members of the team can be expected to have the same level of knowledge and experience, it is the responsibility of the audit engagement partner to ensure that collectively the team has the appropriate competences, and that external specialists, or experts, are engaged as required to meet the needs of engagement circumstances. For example, expertise may be needed in relation to such matters as:

- The valuation of complex financial instruments, land and buildings, intangible assets, assets acquired and liabilities assumed in business combinations and assets that may have been impaired;
- The actuarial calculation of liabilities associated with insurance contracts or employee benefit plans;
- The estimation of oil and gas reserves;
- The valuation of environmental liabilities, and site clean-up costs;
- The interpretation of contracts, laws and regulations;
- The analysis of complex or unusual tax compliance issues; and
- The entity's information systems, especially if the entity is considered to be information technology dependent.

- ~~51-62.~~ ~~the team may require skills in information technology or in particular financial reporting issues, which~~ Expertise may be obtained either from within the audit firm or from external sources. If specialists or experts are involved, it is important, as with other members of the engagement team, that their work is appropriately directed, supervised and reviewed.
- ~~52.~~ ~~The need to involve information technology specialists increases with the complexity of information systems and the degree to which the entity is IT dependent.~~
63. The appropriate development of professional knowledge and skills begins with the Initial Professional Development of the aspiring professional accountant. The necessary competences for auditors are described in International Education Standards (IESs) issued by the IAESB. The recent exposure draft of IES 8 categorizes these between technical competence, professional skills, and professional values, ethics and attitudes. It also recognizes the professional development needed to foster and maintain professional competence for those currently serving as engagement partners, especially for those serving on audits involving more complex industries, operations, or reporting requirements.⁸ Professional skills include interpersonal and communications skills. Then, further specialization by the professional accountant to perform the role as an auditor is achieved through Continuing Professional Development and additional auditing work experience. Continuing Professional Development of professional competence and lifelong learning are critical if auditors are to continue to meet the expectations of their clients and the public.⁹
- ~~53-64.~~ In many countries, public sector audit institutions have to keep within fixed limits for how much they may spend on staff resources. There may also be regulations that impact recruitment of staff and the salaries that can be paid. This can mean it is challenging for certain audit institutions to recruit and retain sufficient numbers of high-quality staff to consistently achieve audit quality.

1.4.2 Partners and Staff Understand the Entity's Business

- ~~54-65.~~ A sound understanding of the entity, its business and the industry in which it operates is key to the auditor being able to assess the risks of material misstatement in the financial statements to appropriately focus audit procedures and to evaluate the findings from them. It is also ~~underlies~~ necessary for the exercise of professional skepticism and the ability to make appropriate audit judgments.
66. Industry knowledge, including an understanding of relevant regulations and accounting issues, can be especially important for clients in, for example, the financial services industry. However, it is important that knowledge areas are not so narrow that they prevent the auditor from seeing broader issues. Auditors can acquire general business knowledge from undertaking non-audit work and

⁸ Competence areas and learning outcomes for the aspiring professional accountant are provided in IES 2, Initial Professional Development – Technical Competence; IES 3, Initial Professional Development – Professional Skills; and IES 4, Initial Professional Development – Professional Values, Ethics, and Attitudes; while, competence areas and learning outcomes for the engagement partner are provided in IES 8, Professional Development for Engagement Partners Responsible for Audits of Financial Statements; IES 8, *Competence Requirements for Audit Professionals*. An exposure draft of a proposed revised IES 8, *Professional Development for Engagement Partners Responsible for Audits of Financial Statements*, was issued on August 9, 2012. The proposed revised version specifies the learning outcomes that demonstrate the professional competence required of a newly appointed engagement partner.

⁹ The revised IES 8 recognizes the auditor's need for continuous improvement of competence by first identifying learning outcomes and then requiring Continuing Professional Development in competence areas required of engagement partners who are responsible for audits of financial statements.

from exposure to different clients in different industries. This allows them to stand back from the specifics of a particular entity's business and reflect upon their broader knowledge of business issues, risks, and control systems.

~~67.~~ Audits of smaller entities by sole practitioners and SMPs are often conducted on site by experienced personnel who have been involved with the entity for a number of years. While such personnel usually have a good knowledge of the entity's business, there may be threats to their objectivity and skepticism.

~~55.~~

1.4.3 *Partners and Staff Make Reasonable Judgments*

~~56-68.~~ Auditing is a discipline that relies on competent individuals using their experience and the values of integrity, objectivity and skepticism to enable them to make reasonable professional judgments that are supported by the facts and circumstances of the engagement.

~~57-69.~~ Making reasonable judgments may involve partners and staff:

- Identifying the issue;
- Applying knowledge of business, financial accounting and reporting and information technology;
- Researching the topic and considering different perspectives;
- Evaluating alternatives in the light of the relevant facts and circumstances;
- Considering whether a suitable process was followed in reaching a conclusion and whether sufficient appropriate audit evidence exists to support it;
- Consulting, as appropriate; and
- Documenting the conclusion and the rationale for it.

1.4.4 *The Audit Engagement Partner Is Actively Involved in Risk Assessment, Planning, Supervising, and Reviewing the Work Performed*

~~58-70.~~ As engagement partners are responsible for the audits they undertake, it is important that they are directly involved in planning the audit, evaluating the evidence obtained and in reaching final conclusions.

~~59-71.~~ While much of the detailed audit work may be delegated to less experienced staff, audit engagement partners need to be accessible to them in order to provide timely input as the audit progresses.

~~60-72.~~ Some believe that disclosure of the engagement partner's name in the auditor's report should be required for all entities, as it would provide the engagement partner with a greater sense of personal accountability, as this individual is ultimately responsible for the conduct of the audit. In many jurisdictions this is already required, usually by a requirement for a personal signature. Others believe that such a requirement would have no impact on an engagement partner's sense of accountability, and there are potential impediments of such a requirement. In particular, with respect

to a perceived reduction in the responsibility of the firm and the possibility of increased legal liability for the engagement partner in some jurisdictions.

1.4.5 *Staff Performing Detailed “On-Site” Audit Work Have Sufficient Experience, Their Work Is Appropriately Directed, Supervised and Reviewed, and There Is a Reasonable Degree of Staff Continuity*

~~64-73.~~ The structure of many audit firms is hierarchical, especially larger audit firms – firms are often described as having a “pyramid structure” – and the make-up of many audit teams for individual engagements generally reflects this structure. As a result, much of the detailed “on-site” audit work is likely to be performed by staff who are relatively inexperienced; indeed, many may still be completing an accounting qualification. However, experience is needed for staff to make reasonable professional judgments.

~~62-74.~~ Furthermore, management often seek audit staff continuity as involving the same staff members on an audit, one year after another, is likely to assist them in understanding the entity’s business and systems. Some believe that this is likely to result in effective responses to business risks of material misstatement in the financial statements, as well as audit efficiency. However, prolonged involvement may result in a lack of skepticism and threats to auditor independence.

1.4.6 *Partners and Staff Have Sufficient Time to Undertake the Audit in an Effective Manner*

~~63-75.~~ Partners and staff often have responsibilities other than the audit of a single entity, and audits can be undertaken to challenging timetables. Planning is important, both at the level of an individual audit and at the level of the audit firm, to ensure that adequate resources are available to gather sufficient appropriate audit evidence and to interact appropriately with management and those charged with governance.

~~64-76.~~ Audit firms are usually profit-making entities and the profitability of an audit firm is influenced by the relationship between the audit fees charged and the cost involved in gathering sufficient appropriate audit evidence. Audit engagement partners are usually accountable within their audit firms for the financial return on the audits they perform and, if audit fees are restricted by management, this may put pressure on the engagement team to change the nature and timing of audit procedures or reduce testing. This, in turn potentially threatens audit quality.¹⁰

1.4.7 *The Audit Engagement Partner and Other Experienced Members of the Audit Team Are Accessible to Management and Those Charged With Governance*

~~65-77.~~ It is important that the audit engagement partner is accessible to senior members of management and those charged with governance. Regular contact allows the audit engagement partner to be well briefed on developments in the entity’s business as well as raise issues related to the audit on a timely basis.

¹⁰ Ethics requirements (for example, paragraph 240.2 of the IESBA Code) often describe this threat and require it to be evaluated and, where appropriate, safeguards applied.

1.5 Knowledge, Experience and Time – Firm Level

~~66-78.~~ The audit firm’s policies and procedures will impact the required knowledge and experience of audit engagement partners and other members of the engagement team, and the time available for them to undertake the necessary audit work. Key attributes are:

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
Knowledge, Experience, and Time	Section 1.4	Section 1.5	Section 1.6
Audit Process and Quality Control Procedures	Section 1.7	Section 1.8	Section 1.9

- Partners and staff have sufficient time to deal with difficult issues as they arise
- Engagement teams are properly structured.
- Partners and more senior staff provide less experienced staff with timely appraisals and appropriate coaching or “on-the-job” training.
- Sufficient training is given to audit partners and staff on audit, accounting and, where appropriate, specialized industry issues.

1.5.1 Partners and Staff Have Sufficient Time to Deal with Difficult Issues as They Arise

~~67-79.~~ Partners and senior staff usually work on a number of audits often with similar reporting timetables. This can lead to concentrated periods of activity. Partners and senior staff also often undertake non-audit services for clients or other activities within the audit firm. It is important that firms anticipate, as best they can, and manage possible time conflicts when allocating responsibilities. Firm management need to proactively monitor work levels to reduce the risk that an unacceptable burden is put on individual partners or staff.

1.5.2 Engagement Teams Are Properly Structured

~~68-80.~~ Human resource allocation also needs to take account of risk. A danger exists that the most competent partners and staff will be allocated to the firm’s largest most prestigious clients and, as a result, will not be available to audit other clients where the risks that the financial statements are misstated may be greater.

~~69-81.~~ An audit firm needs to allocate its resources so that engagement teams have the expertise and time to undertake particular audits. This involves allocating partners and senior staff who have both an appropriate knowledge of the industry in which the client operates and its applicable financial reporting framework, and sufficient time to be able to perform quality audits.

~~70-82.~~ Allocating resources involves the firm gathering information on:

- ~~Knowledge.~~ Skills and experience;
- Estimated time commitments; and
- Periods of service – to facilitate compliance with ethics requirements, for example, in relation to the rotation of audit partners.

~~74-83.~~ Audits of smaller entities are not mandated in some countries. This can mean that in such countries—especially where audits of smaller entities are largely performed by SMPs—it is

challenging for SMPs that have only a small number of audit clients to retain partners and staff with relevant audit knowledge and experience.

1.5.3 *Partners and More Senior Staff Provide Less Experienced Staff with Timely Appraisals and Appropriate Coaching or “On-the-Job” Training*

~~72-84.~~ An audit firm’s appraisal process is an important aspect of developing an individual’s capabilities. Although it is difficult to measure, audit quality is likely to be improved if it is specifically addressed in the appraisals for both partners and staff. This can be used to promote the exercise of good audit judgment, including consultation on difficult issues.

~~73-85.~~ A distinction can usefully be made between providing staff with periodic performance appraisals and giving coaching and on-the-job training. While appraisals can be used to help identify the absence of an important skill or competence, coaching or on-the-job training can be used to help an individual develop that skill or competency. Coaching and on-the-job training is likely to be especially important in relation to developing key personal characteristics such as integrity, objectivity, rigor, skepticism, and perseverance as well as assisting less experienced staff deal with unfamiliar audit areas.

~~74-86.~~ Being able to coach effectively requires additional skills, knowledge, and experience, and there are not an unlimited number of people within audit firms with the appropriate competences. Such people may have other demands on their time, including “special” or non-audit work, or involvement in the internal management of the firm. It is important that firms provide incentives to their more experienced staff to allocate the necessary time to undertake this important staff development role effectively and, as part of the appraisal process, evaluate them on whether this is achieved.

1.5.4 *Sufficient Training Is Given to Audit Partners and Staff on Audit, Accounting and, Where Appropriate, Specialized Industry Issues*

~~75-87.~~ The profession endeavors to equip auditors with the necessary competence through initial professional development (IPD), comprising training in technical and professional skills and values, ethics and attitudes and practical experience, and continuing professional development (CPD) requirements.

~~76-88.~~ Firms generally provide training in the technical aspects of audit and in the requirements of their audit methodologies. Firms also provide essential practical experience by including trainees in audit teams undertaking audit work.¹¹ Merging learning about the technical aspects of auditing with gaining practical experience is important because formal training is only part of the process by which auditors develop skills and experience.

~~77-89.~~ Professional accountancy bodies—organizations that are members of IFAC have requirements relating to CPD and the development programs used by the firms have the potential to be an important contributor to an auditor’s competence. Such programs often address a wide range of areas relevant to the firm’s business as a whole, such as project management, information technology, and communication skills. It is important that firms dedicate sufficient time, resources

¹¹ IES 8, paragraphs 54 and 59, establishes requirements for practical experience for audit professionals.

and importance to training in audit and accounting matters including, where appropriate, specialized industry issues so as to provide the technical skills needed to support audit quality

1.6 Knowledge, Experience and Time – National Level

~~78-90.~~ National activities can impact the competences of auditors and the time spent. Key attributes are:

- Robust arrangements exist for licensing audit firms/individual auditors.
- Education requirements are clearly defined and training is adequately resourced and effective.
- Arrangements exist for briefing auditors on current issues and for providing training to them in new accounting, auditing or regulatory requirements.
- The auditing profession is well-positioned to attract and retain high-quality individuals.

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
Knowledge, Experience, and Time	Section 1.4	Section 1.5	Section 1.6
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1.6.1 Robust Arrangements Exist for Licensing Audit Firms/Individual Auditors

~~79-91.~~ Auditing is a public interest activity which needs to be performed by suitably qualified individuals working in an appropriate environment. To achieve this, there will commonly be national arrangements for licensing audit firms or individual auditors to perform audits. A register of approved firms and individuals/persons will often be maintained by a competent authority. Authorities will often have the power to revoke the license in defined circumstances.

1.6.2 Education Requirements Are Clearly Defined and Training Is Adequately Resourced and Effective

~~80-92.~~ Criteria for obtaining a license will usually involve educational requirements both for IPD and CPD. Audit quality will be facilitated if educational requirements are clearly defined and sufficient resources are applied to provide ensure necessary training is effective.

~~84-93.~~ The professional skills described in IESs underlie the competences needed to support audit quality. These competences are developed by a combination of theoretical training and practical experience and coaching within audit firms. IESs are written for IFAC member bodies (which may have responsibility for the theoretical training), but do not apply directly to audit firms (which provide the practical experience and coaching). It may assist audit quality if both training organizations and audit firms use the same competence framework.

1.6.3 Arrangements Exist for Briefing Auditors on Current Issues and for Providing Training to Them in New Accounting, Auditing or Regulatory Requirements

~~82-94.~~ In addition to training related to an auditor's IPD, appropriate arrangements within a country for CPD are an important factor in contributing to audit quality. CPD needs to be provided in order that more experienced auditors continue to develop their skills and knowledge related to auditing, and keep informed about changes in the accounting and regulatory requirements.

~~83-95.~~ CPD is particularly important when there are major changes to requirements relating to financial reporting and auditing. This provides an opportunity to brief auditors on the new technical

requirements, to explain the objectives of those changes, and to help create the understanding necessary for the new requirements to be implemented in a cost effective manner.

1.6.4 *The Auditing Profession Is Well-Positioned to Attract and Retain High-Quality Individuals*

~~84-96.~~ The competences of audit partners and staff are a critical factor underlying audit quality. While training is important, some of the required qualities are, to a degree, inherent in the individuals. It is therefore important that individuals with the right qualities are attracted to a career in the auditing profession.

~~85-97.~~ There are likely to be a number of factors that will influence the individuals attracted to a career in the auditing profession, including:

- The status of auditing as a profession in the national environment;
- Perceptions of career opportunities and remuneration incentives;
- The nature of the work, including its role in relation to the public interest; and
- The quality of training provided.

~~86-98.~~ The same factors are likely to influence individuals' decisions to remain in the auditing profession, and pursue an extended career in auditing. In some countries, there is a tendency for large numbers of newly qualified accountants to leave the audit firms and take jobs in business. While this may have a beneficial impact on financial reporting, it can limit the number of experienced staff available to audit firms and thereby jeopardize audit quality.

~~87-99.~~ The status of the auditing profession in a national environment can also impact the respect for auditors and therefore the effectiveness of the audit function. In environments where the audit profession is not well respected or given appropriate authority, auditors will be in a weaker position relative to management. In such circumstances, there may be a lower likelihood that auditors will probe management on significant matters or stand firm on significant audit issues. Conversely, where the profession is highly regarded or is conferred appropriate authority through the relevant mechanisms, it will be easier for auditors to demonstrate professional skepticism and undertake robust audits.

1.7 Audit Process and Quality Control Procedures – Engagement Level

~~88-100.~~ Audits need to be performed in accordance with auditing standards and are subject to the audit firm's quality control procedures, which comply with the IAASB's ISQC1. These provide the foundation for a disciplined approach to risk assessment, planning, performing audit procedures and ultimately forming and expressing an opinion. Sometimes, audit firms' methodologies and internal policies and procedures provide more specific guidance on matters such as who undertakes specific activities, internal consultation requirements, and documentation formats.

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
Knowledge, Experience, and Time	Section 1.4	Section 1.5	Section 1.6
Audit Process and Quality Control Procedures	Section 1.7	Section 1.8	Section 1.9

~~89-101.~~ While auditing standards and the audit firm's methodology will shape the audit process, the way that process is applied in practice will be tailored to a particular audit. Key attributes are:

- The engagement team complies with auditing standards, relevant laws and regulations, and the audit firm's quality control procedures.
- The engagement team makes appropriate use of information technology.
- There is effective interaction with others involved in the audit including, where applicable, internal auditors.
- There are appropriate arrangements with management so as to achieve audit efficiency.
- There is appropriate audit documentation.

1.7.1 *The Engagement Team Complies with Auditing Standards, Relevant Laws and Regulations, and the Audit Firm's Quality Control Procedures*

~~90-102.~~ Auditors are ~~usually often~~ required by national law or regulations to comply with auditing standards. However, not all aspects of the audit process are defined by auditing standards, and audit firms will usually have methodologies that provide further specification. Even within the structure created by auditing standards and firm methodologies, there is flexibility for the audit team in terms of what specific audit work is performed, how it is undertaken in practice, and the nature and timing of interactions with management. The way that the work is performed in practice can be an important factor in both effectiveness and efficiency.

1.7.2 *The Engagement Team Makes Appropriate Use of Information Technology*

~~94-103.~~ The automation of information systems provides opportunities for auditors to gather audit evidence both more effectively and more efficiently; for example, through the use of computer-assisted audit techniques including file interrogations and the use of test data. These techniques have the advantage that greater coverage of transactions and controls can be achieved. However, sometimes the use of such techniques requires the involvement of specialists, which can be time consuming, especially in the first year that they are used.

~~92-104.~~ Information technology platforms within audit firms have an effect on the way auditors conduct an audit and record the work performed. Increasingly, audit software is provided to assist engagement teams to implement a firm's methodology. While this can result in efficiencies and improved quality control processes, risks to audit quality associated with their use include:

- Over-emphasizing compliance with the audit firm's audit software rather than encouraging thinking about the unique characteristics of the entity being audited; ~~and~~
- New staff spending too much of their time learning how to use the firm's audit software rather than understanding auditing concepts; ~~and~~
- ~~Partners and experienced staff reviewing audit work from remote locations and thereby reducing the opportunities for mentoring and on-the-job training.~~

~~105.~~ While ~~having p~~Partners and experienced staff reviewing audit work from remote locations ~~and thereby might reduce~~ing the opportunities for mentoring and on-the-job training, it has the potential benefits of:-

- permitting more effective review of audit work where engagement team members are located across different time zones;

- permitting more effective review of audit work where engagement team members are working across many sites; and
- providing a more effective means of undertaking supplemental reviews of audit work, after initial reviews have been performed.

~~93-106.~~ Information technology also has an effect on the way auditors communicate, both within audit teams and with management and those charged with governance. For example, e-mails and other professional service automation tools are increasingly being used. While e-mail generally increases accessibility, especially on an international basis, e-mails can have limitations. In particular, there may be a reduced opportunity to obtain useful audit evidence from e-mail exchanges than from the richer interaction that comes through having a fuller open discussion with management. Depending on the circumstances, e-mail might also make it easier for management to provide inaccurate or incomplete responses to the auditor's questions or be less forthright with information if management is motivated to do so.

1.7.3 *There Is Effective Interaction with Others Involved in the Audit Including, Where Applicable, Internal Auditors*

~~94-107.~~ Most large entities will have divisions, subsidiaries, joint ventures or investees accounted for by the equity method (components), and one or more components are frequently audited by audit teams other than the group audit team. If effective two-way communication between the group engagement team and the component auditors does not exist, there is a risk that the group engagement team may not obtain sufficient appropriate audit evidence on which to base the group audit opinion. Clear and timely communication of the group engagement team's requirements forms the basis of effective two-way communication between the group engagement team and the component auditor¹².

~~95-108.~~ Others involved in the audit could include specialists and experts (for example, IT specialists), or, in a group context, the auditors of components. Where others are involved in the audit, it is important that:

- The engagement team clearly communicates with them about the work to be performed;
- Others involved clearly communicate the findings from the work performed; and
- The engagement team determines that the work performed is adequate for its purpose and reacts appropriately to the findings.

~~109.~~ Many large entities will have an internal audit function. It is likely to be important for both audit efficiency and effectiveness for there to be effective interaction between the external and internal auditors. For example, the internal audit function is likely to have obtained insight into the entity's operations and business risks that will provide valuable input into the auditor's understanding of the entity and risk assessments or other aspects of the audit.

~~96-110.~~ Group management usually expects the group auditor to co-ordinate the work undertaken on components efficiently. Some believe that this can be facilitated if the audits of components are undertaken by the same audit firm or firms within the same audit network or association. The firm's

¹² Refer to ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*, paragraph A57.

geographic reach, and therefore its ability to provide audit coverage for subsidiaries and other components of the group, can therefore be important. Others believe that having a number of different audit firms involved in a group audit provides an opportunity for a range of views on the risks of the entity, and appropriate audit responses, to be considered.

1.7.4 *There Are Appropriate Arrangements with Management so as to Achieve Audit Efficiency*

~~97.111.~~ Management may have an interest in ensuring that the audit is completed as quickly as possible and the disruption to the entity’s ongoing operations is minimized. While auditors need to gather sufficient appropriate perform an effective audit evidence in all circumstances, audit efficiency can be ~~achieved~~ enhanced through:

- Rigorous planning, including, where appropriate, agreeing with management information needs and timetable;
- Timely engagement with management to resolve issues identified during the audit;
- Striving to meet agreed timelines and reporting deadlines; and
- Avoiding, as far as possible, duplicate inquiries of management on the same matter from different engagement team members.

~~98.~~ Group management usually expects the group auditor to co-ordinate the work undertaken on components efficiently. Some believe that this can be facilitated if the audits of components are undertaken by the same audit firm or firms within the same audit network or association. The firm’s geographic reach, and therefore its ability to provide efficient audit coverage for subsidiaries and other components of the group, can therefore be important. Others believe that having a number of different audit firms involved in a group audit provides an opportunity for a range of views on the risks of the entity, and appropriate audit responses, to be considered.

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1.7.5 *There Is Appropriate Audit Documentation*

~~99.112.~~ ISAs require documentation to be prepared sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing and extent of the procedures performed, the results of those procedures, the significant matters arising and the conclusions reached. This documentation supports quality control activities both within the audit team, before the audit is completed, and by others who review the quality of work performed.

1.8 **Audit Process and Quality Control Procedures – Firm Level**

~~100.113.~~ The audit firm’s policies and procedures will impact the audit process. Key attributes that contribute to audit quality are:

- The audit methodology is adapted to developments in professional standards and to findings from internal quality control reviews and external inspections.
- The audit methodology encourages individual team members to apply professional skepticism and exercise appropriate professional judgment.

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
Knowledge, Experience, and Time	Section 1.4	Section 1.5	Section 1.6
Audit Process and Quality Control Procedures	Section 1.7	Section 1.8	Section 1.9

- The methodology requires effective supervision and review of audit work.
- The methodology requires appropriate audit documentation.
- Rigorous quality control procedures are established and audit quality is monitored and appropriate consequential action is taken.
- Where required, effective engagement quality control reviews are undertaken.

1.8.1 *The Audit Methodology Is Adapted to Developments in Professional Standards and to Findings from Internal Quality Control Reviews and External Inspections*

~~114.~~ The audit firm's audit methodology should not remain static but should evolve with changes in professional standards, business processes, and the environment. Importantly, continual and timely improvements to the firm's audit methodology and tools should be made to respond to findings from internal reviews and regulatory inspections.

~~404-115.~~ In demonstrating a commitment to continuous improvement, audit firms should examine reasons for poor quality audits in order to identify systemic issues, and respond accordingly by taking actions to improve their methodologies and processes.

1.8.2 *The Audit Methodology Encourages Individual Team Members to Apply Professional Skepticism and Exercise Appropriate Professional Judgment*

~~402-116.~~ Most audit firms use methodologies to assist staff in achieving an efficient and effective audit and for quality control processes. These methodologies ~~are sometimes in the form~~ involve the use of audit software that supports decisions and generates electronic working papers that can be viewed at remote locations.

~~403-117.~~ Such methodologies can be an effective mechanism for achieving consistent compliance with auditing standards and for checking whether all necessary steps in the audit process have been performed. Methodologies also assist with documentation and, if in an electronic form, with the rapid sharing of information, including with specialists at remote locations.

~~404-118.~~ However, there is a risk that too high a level of prescription in audit methodologies will have negative implications for other elements of audit quality. Highly prescriptive methodologies may arise from threats of litigation or overly compliance-based approaches to auditor regulation and inspections. Examples of the risk to audit quality include:

- ~~If~~ if compliance with a very prescriptive methodology is over-emphasized, there is a risk that insufficient emphasis will be given to experienced staff tailoring the specified audit procedures to the circumstances and considering whether further procedures need to be performed;:-
- ~~Over~~ over-emphasizing the process by which an audit is performed may detract from experienced audit partners and staff making important judgments;:-
- ~~Reducing~~ reducing too far the freedom of action of staff may undermine the motivation of these individuals and cause them not to pursue a career in auditing; and
- the potential to distance both partners and staff from the company being audited.

~~405. The trend to use audit software also has the potential to distance both partners and staff from the company being audited. In part, this trend increases the risk that the information and audit evidence that have historically been obtained by spending time with company personnel, “walking the floor” and observing and inspecting the company’s operations may not be obtained.~~

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1.8.3 *The Methodology Requires Effective Supervision and Review of Audit Work*

~~406,119. Much of the detailed audit work may be performed by staff who are relatively less experienced. In such circumstances, it is vital that their work, whether performed ‘on-site’ or ~~offshore~~ elsewhere, including the practice of offshoring, is supervised and reviewed by experienced staff, manager, and partners.~~

~~407,120. Some modern methodologies provide the opportunity for electronic, off-site review of working papers, which can enable audit issues to be shared and considered efficiently, especially when dealing with different countries and across different time zones. However, off-site review may not always be an effective means; of assessing whether staff have undertaken the audit thoroughly and demonstrated an appropriate degree of skepticism; and. Furthermore, ~~electronic, off-site review is unlikely to assist with the coaching or on-the-job training that is vital~~ for developing the skills and competences of less experienced staff.~~

1.8.4 *The Methodology Requires Appropriate Audit Documentation*

~~408,121. Audit documentation performs a number of roles, including:~~

- Assisting the engagement team to plan and perform the audit.
- Assisting members of the engagement team responsible for supervision to direct and supervise the audit work.
- Enabling the engagement team to be accountable for its work.
- Retaining a record of matters of continuing significance to future audits.
- Enabling the conduct of intra-firm quality control reviews and inspections, and external inspections in accordance with applicable legal, regulatory or other requirements.

~~409,122. Documentation of the rationale for an significant audit judgments is likely to increase the rigor, and therefore the quality, of that judgment. The process of ~~committing to writing~~ documenting the issues and how they have been resolved is likely to improve the rigor of the auditor’s thought process and the validity of the conclusions reached.~~

1.8.5 *Rigorous Quality Control Procedures Are Established and Audit Quality Is Monitored and Appropriate Consequential Action Is Taken*

~~440,123. Quality control procedures need to be established to provide the audit firm with assurance that:~~

- The firm complies with professional standards and applicable legal and regulatory requirements, and

- Reports issued by the firm or engagement partners are appropriate in the circumstances¹³.

124. Quality control procedures will include monitoring and taking remedial action when needed. Auditing involves compliance with standards and internal firm policies and procedures. It also involves difficult decisions and judgments made by staff at different levels of experience and sometimes under time pressure.

444.125. Monitoring audit quality within an audit firm is an important aspect of identifying emerging risks and opportunities, and ensuring that standards are being adhered to and that the partners and staff are performing appropriately.

442.126. Some audit firms operate internationally through a network of firms. Network firms often share common methodologies and quality control and monitoring policies and procedures. Some networks also share guidance in relation to values, ethics, and attitudes, and have programs to enhance the knowledge and experience of partners and staff.

443.127. In addition to internal processes to monitor audit quality, audits may be subject to external review ~~by audit regulators~~. The results of these ~~external reviews (including and inspections performed by independent audit regulators)~~, provide important feedback that should lead to actions that contribute to enhancing audit quality.

444.128. In addition to addressing any shortcomings that have been identified on individual audits, it is important that audit firms ~~identify take appropriate actions to address~~ systemic issues revealed by both internal and external monitoring activities and take appropriate action.

1.8.6 Where Required, Effective Engagement Quality Control Reviews Are Undertaken

445.129. Engagement quality control reviews (EQCRs) allow for an objective evaluation of the significant judgments made by the engagement team and the conclusions reached in formulating the auditor's report. They are required to be performed on audits of listed companies and those other audit engagements for which the audit firm considers them appropriate, such as audits of public interest entities.

446.130. To be effective, EQCRs involve discussion of significant matters and conclusions, a review of selected engagement documents, and a review of the financial statements. They need to be performed by individuals with the necessary experience, authority and time. EQCRs require ~~the cooperation of~~ appropriate liaison between the review partner and the engagement partner so that they can be performed on a timely basis and allow the engagement team to respond appropriately to findings.

¹³ The IAASB has issued ISQC 1, which sets out those activities in which firms are required to develop policies and procedures and thereby meet this objective.

1.9 Audit Process and Quality Control Procedures – National Level

447-131. National audit regulatory activities can impact the audit process. Key attributes are:

- Auditing standards are promulgated that make clear the underlying objectives as well as the specific requirements that apply.
- Bodies responsible for external audit inspections consider relevant attributes of audit quality, both within audit firms and on individual audit engagements.
- Effective systems exist for investigating allegations of audit failure and taking disciplinary action when appropriate.

	Engagement Level	Firm Level	National Level
Values, Ethics, and Attitudes	Section 1.1	Section 1.2	Section 1.3
Knowledge, Experience, and Time	Section 1.4	Section 1.5	Section 1.6
Audit Process and Quality Control Procedures	Section 1.7	Section 1.8	Section 1.9

1.9.1 *Auditing and Other Standards Are Promulgated that Make Clear the Underlying Objectives as Well as the Specific Requirements that Apply*

132. Auditing and other requirements may be imposed by law or regulations or mandated through the national professional accountancy organization. It is important that such requirements are high-quality and make clear the underlying objectives of the audit. ISAs, as issued by the IAASB, contain objectives, requirements, and application and other explanatory material.

133. It is important that standards are revised in response to feedback received about their use and implementation. However, it is important for standard-setters to be cognizant of the impact that regular revisions to standards may have on auditors' training and implementation needs in using the standards.

448-134. ISAs are issued by the IAASB. The International Ethics Standards Board for Accountants (IESBA) sets high-quality ethical standards for professional accountants through the development of a robust, internationally appropriate Code of Ethics for Professional Accountants; while the International Accounting Education Standards Board (IAESB) develops and enhances professional accountancy education—encompassing knowledge, skills, values, ethics, and attitudes—through the promulgation of International Education Standards (IESs). There is widespread adoption of these standards at a national level.

449-135. IFAC requires its member bodies to take actions to adopt and implement ISAs in their jurisdictions, and to assist in their implementation, depending on the member bodies' responsibilities in national environments. In some countries, the ISAs are modified to take account of, or are supplemented by additional, national requirements.

1.9.2 *Bodies Responsible for External Audit Inspections Consider Relevant Attributes of Audit Quality, Both Within Audit Firms and on Individual Audit Engagements*

120. ~~In many countries, arrangements exist for the independent monitoring of audit quality either by a separate audit firm (a peer review), a professional accountancy organization (which sometimes has been delegated responsibility by a regulator), or by independent audit inspectors. Increasingly, law and regulations provide that the inspections of audits of listed companies, and sometimes those of~~

~~other public interest entities, are undertaken by an independent audit regulator with a mandate to protect the public interest.~~

~~124,136.~~ External audit inspections provide an opportunity for evaluating auditors' compliance with auditing standards, and depending on their mandate, other aspects of audit quality. Actions taken by audit firms to address weaknesses identified by audit inspectors can lead to improvements in audit effectiveness and, where the results of audit inspections are published, will lead to greater awareness among stakeholders about audit quality issues. Over a period of time, the findings from external audit inspections need to be captured and fed back to standard setters.

~~122.~~ A number of independent audit regulators are relatively new organizations. In an international context, the activities of the International Forum of Independent Audit Regulators (IFIAR) facilitate knowledge sharing and promote greater coordination among audit regulators.⁴⁴

1.9.3 *Effective Systems Exist for Investigating Allegations of Audit Failure and Taking Disciplinary Action When Appropriate*

~~123.~~ The requirements of auditing and other relevant standards are most effective if they are properly enforced. This involves investigation of allegations of audit failure and, where appropriate, disciplinary action being taken.

~~124.~~ As well as acting as an incentive to audit firms to comply with applicable standards, effective disciplinary arrangements give other stakeholders confidence in the quality of audit. Effective disciplinary arrangements involve those responsible for investigation and disciplinary functions having a clear mandate and sufficient resources to undertake their work.

~~125,137.~~ Investigation and disciplinary action can be undertaken by professional accountancy organizations. However, as is the case with audit inspection, in relation to listed companies and other public interest entities, it is increasingly being undertaken by independent audit regulators.

~~126,138.~~ Audit failures can be difficult to define, especially as so much of an audit involves judgment, and criteria in laws and regulations are sometimes vague and difficult to enforce. The effectiveness of disciplinary activities is increased when clear criteria have been established as to what represents an audit failure.

~~127,139.~~ Authorities also need a range of sanctions available to them, including the power to revoke the license of audit firms or individual auditors in defined circumstances. While such actions may be appropriate in extreme cases, the regulatory process is enhanced when more proportional sanctions are also available for lesser issues. These may include fines and mandatory retraining.

~~128.~~ Transparency through the timely disclosure of investigations and disciplinary actions has the potential to provide important feedback to auditors and audit firms, in relation to matters that may enhance audit quality.

~~There will also be benefit in audit firms analyzing the results from internal inspections and investigations in order to learn from deficiencies noted and improve their methodologies and procedures to prevent repeat occurrences.~~

⁴⁴ Currently, IFIAR has over 40 members. Further information about its activities can be found on its website: www.ifiar.org.