An External Auditor's Guide to

Improving Audit Quality Using an Individual Recognition and Accountability Framework

2019

About this guide

This guide has been developed by CPA Australia on behalf of the Australian Auditing and Accounting Public Policy Committee (APPC), which comprises representatives of BDO, Deloitte, EY, Grant Thornton, KPMG, PwC, Chartered Accountants Australia and New Zealand (CA ANZ), CPA Australia and the Institute of Public Accountants (IPA). The APPC is committed to playing a part in improving the quality of audits across the profession and hopes this guide will be a useful tool for firms of any size.

In determining effective mechanisms to improve audit quality, the APPC network firms considered what, in their experience, has had the biggest impact on audit quality. They agreed that one of the key drivers of improvement in audit quality was the use of recognition and accountability mechanisms that focus on individuals with audit-related leadership positions. Both mechanisms contribute to audit quality: recognition emphasises incentives or rewards for good audit quality, while accountability focuses on the consequences of poor audit quality. This project sought to understand current recognition and accountability frameworks and develop a guide that could be shared across the profession.

This guide is not designed to create new 'rules' or a one-size-fits-all framework for firms to follow. Instead, it aims to cross-pollinate ideas and learning by outlining the ways firms can approach recognition and accountability frameworks. To inform the guide, interviews were conducted and many different key performance indicators (KPIs) and firms' cultures were observed. The material gathered has been distilled into this guide, which will:

- Facilitate and initiate innovation and growth across the profession by sharing the best elements of current practice.

- Provide a resource that is scalable for small and mid-tier firms.

How to use this guide

Firms can use this guide as a catalyst for developing a recognition and accountability framework or reviewing their current framework and related processes. They can consider whether their processes may be enhanced by implementing or adapting some of the mechanisms suggested in this guide. The type of mechanisms that will be effective will vary between firms and change over time. As such, the framework outlined in this guide needs to be adapted to meet the needs of each firm and its leaders. It should also be reviewed regularly to ensure it remains effective.

Contents

Why have an Individual Recognition and Accountability Framework for Audit Quality?

To deliver quality audits of financial reports, the individuals conducting those audits need to be motivated to strive for high quality and be aware that they must take responsibility when the standard of work falls short of expectations. Individuals working on audit engagements need to understand the level of quality needed to deliver audit outcomes in which users can have confidence. They must also seek to achieve that audit quality consistently. A firm's system of quality management is the foundation for enabling individuals to achieve quality audit outcomes.

The purpose of an Individual Recognition and Accountability Framework for Audit Quality is to provide:

1. Incentives or rewards for good or great quality audit outcomes

2. Consequences where audit quality falls short of expectations.

While all members of an audit engagement team play their part in achieving audit quality, this guide focuses on those directly responsible for audit quality at the engagement level, the Audit Engagement Leader and the Audit Engagement Quality Reviewer, as well as those responsible for setting the 'tone at the top' when it comes to audit quality at a practice level, such as the Audit Practice Leader or Business Unit Leader (referred to as the Audit Practice Leader in this guide). This guide will also be relevant to other people who support audit quality, including leaders with risk responsibilities or experts in particular fields. However, these individuals have not been separately addressed in this guide as their roles will vary significantly between firms and engagements.

Audit leaders must meet the quality management requirements for audit engagements under ISA 220/ASA 220 *Quality Management for an Audit of Financial Statements* and relevant aspects of their firm's quality management system to satisfy the requirements of ISQM 1/ASQM 1 *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*. These standards are principles-based and outline the broad elements of effective quality management. However, for rewards and consequences to be effective drivers for individuals, it is important to understand the individuals' motivations, and to tailor the rewards and consequences to suit them.

To be effective, the framework must be flexible and responsive to firm, office and individual characteristics and circumstances, so the drivers of audit quality resonate with the individuals involved and genuinely motivate the behaviours sought. The framework also needs to be practical so it can be effective at the grassroots level rather than simply being a box-ticking compliance exercise.

Context Within a System of Quality Management for Audits

An Individual Recognition and Accountability Framework for Audit Quality fits within a firm's or network's overall quality management system. The information sources that feed into the Individual Recognition & Accountability Framework include:

- Monitoring of audit quality outcomes, which uses information from:

    – Audit quality review outcomes, such as:

        ο External inspections conducted by regulators (primarily the Australian Securities and Investments Commission (ASIC), and the Australian Taxation Office (ATO)) or professional bodies

        ο Internal reviews conducted by a national or international network, a local firm, an office or a peer from another firm, focusing on ISQM 1/ASQM 1 requirements

    – Independence monitoring

    – Engagement team feedback

    – Audit quality indicators or metrics (such as partner hours or the timing of audit work)

    – Financial report restatements for audit clients

- Root cause analysis, which examines:

    – Causal factors for negative and positive external or internal review outcomes

    – Remedial action plans, which identify individual and firm-wide actions to address root causes

Implementation and monitoring of the Individual Recognition and Accountability Framework to ensure it is has been implemented and is effective in rewarding high quality audits and addressing shortcomings in audit quality.

The diagram below illustrates the relationship between these components of a firm's or network's audit quality system and the Individual Recognition & Accountability Framework.
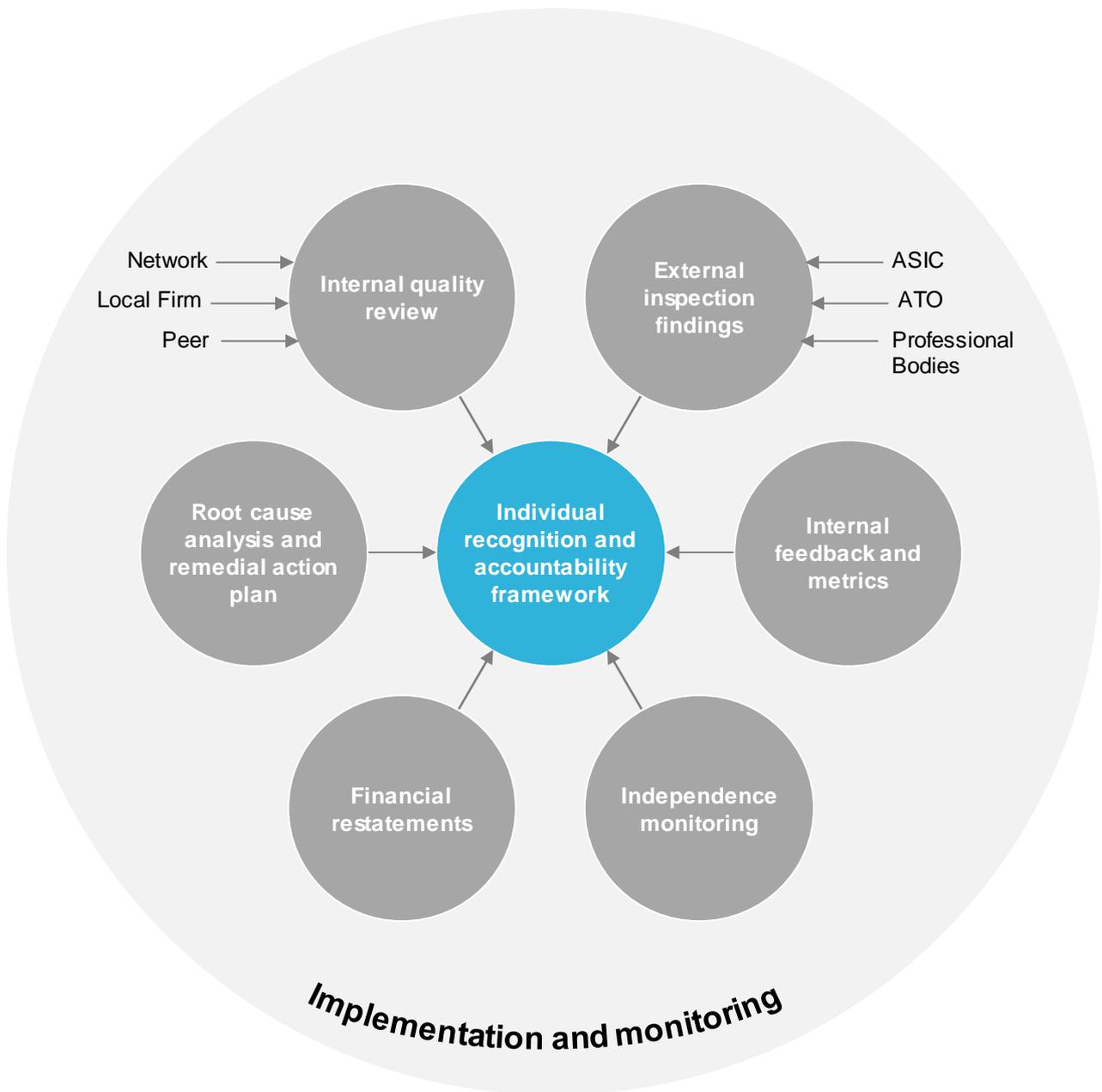
The Process for Individual Recognition and Accountability for Audit Quality

While individual recognition and accountability for audit quality draws on the outcomes of other parts of the audit quality system, an effective framework would incorporate the following process.

| Set expectations about audit quality | Establish accountability and recognition mechanisms | Monitor audit quality outcomes | Implement consequences and rewards | Monitor and review effectiveness |

1. Set expectations about audit quality, which involves identifying:

   a. Who will be accountable; namely, those who create the 'tone at the top' and have an impact on audit quality

   b. What they will be accountable for, which should be reflected in the goals for each role

   c. When assessments of audit quality outcomes and behaviours will occur

2. Establish accountability and recognition mechanisms, which involves:

   a. Identifying indicators and measures of audit quality for each audit leadership role that can be captured systematically

   b. Transparently communicating the expectations regarding audit quality and the measures that will be used to evaluate it

3. Monitor audit quality outcomes, which involves:

   a. Putting systems in place to capture quantitative and qualitative data on audit quality

   b. Assessing and rating audit quality outcomes and behaviours

4. Implement consequences and rewards to drive audit quality through:

   a. Recognition – rewards for leadership in audit quality and consistently high audit quality outcomes, including:

      ο Non-financial recognition when expectations are consistently exceeded

      ο Positive adjustments to performance-related remuneration

   b. Accountability – consequences for poor audit quality outcomes, including:

      ο Intervention when necessary to rectify or prevent further harm, protect the public interest or mitigate liability risk

      ο Non-financial consequences when expectations are not met

      ο Negative adjustments to performance-related remuneration

   These rewards (recognition) and consequences (accountability) can be non-financial or financial, and should be scalable relative to the significance, positive or negative, of the audit quality outcome

5. Monitor and review the effectiveness of the framework by asking the following questions:

   a. Does it maintain and improve audit quality?

   b. Are new measures or mechanisms needed to address audit quality outcomes and identified root causes?

1.   Set Expectations about Audit Quality

Who will be accountable?

The framework focuses on ensuring that audit leaders are motivated to deliver and help the teams supporting them deliver the required audit quality.

The following roles are specifically considered in this guide:

- Audit Practice Leader (PL): A PL is responsible for implementing an effective audit quality management system. They are also key to setting 'the tone at the top' when it comes to audit quality for the business unit they oversee. The root causes of audit quality often stem from the culture of the firm as well as structural and operational enablers overseen by these individuals.

- Audit Engagement Leader (EL): An EL is responsible for overall audit quality on individual audit engagements.

- Audit Engagement Quality Reviewer (EQR): An EQR, where appointed, is responsible for objectively evaluating the significant judgements made by the engagement team and the conclusions it reached in formulating the auditor's report. An EQR has a key quality role, providing a real-time, independent challenge to engagement teams before the audit is completed.

The framework could be extended to other roles within the firm as appropriate. This includes other leaders with responsibility for audit quality or other levels of responsibility within the audit engagement team.

It is critical that the goals and performance criteria are aligned between these different roles so that they are complementary and not at cross-purposes.

What will audit leaders be accountable for?

Audit leaders should be accountable for achieving audit quality objectives. Their individual goals should be aligned to these objectives. To ensure that a balanced view on audit quality performance is used when assessing audit leaders, the relevant objectives should relate to audit quality outcomes that address each of the elements of quality management in ISQM 1/ASQM 1 and ISA 220/ASA 220.

The components of quality management are:

- Governance and leadership

- The firm's risk assessment process

- Relevant ethical requirements

- Acceptance and continuance of client relationships and specific engagements

- Resources

- Engagement performance

- Information and communication

- The monitoring and remediation process.

- Monitoring and remediation process
- Governance and leadership
- Information and communication
- System of quality management
- Risk assessment process
- Engagement performance
- Relevant ethical requirements
- Resources
- Acceptance and continuance of client and engagements

When should audit quality be monitored?

Assessments based on the information gathered should be conducted periodically. At a minimum, this would occur annually through a formal mechanism so that all related information can be collated and a balanced picture considered.

In addition to this formal process, there may be instances where a timely reactive response is required to address triggering events, such as a financial report restatement, withdrawal of an auditor's report or a personal independence issue.

2. Establish Accountability and Recognition Mechanisms

The indicators and measures of audit quality that need to be captured and monitored should reflect outcomes and behaviours identified through:

- An internal review by an office, firm or network, which can be done:

    - Through live reviews while the engagement is in progress. This targets high-risk engagements and high-risk areas, and provides the EL with real-time feedback on planning, controls and substantive work

    - On completion of the engagement but before signing the auditor's report

    - After the auditor's report has been signed. This assesses whether the quality management required by ISA 220/ASA 220 and the requirements of the auditing standards have been applied appropriately

- An external inspection conducted by a regulator or professional body (after the auditor's report is issued)

- Data on metrics or audit quality indicators, which involves identifying thresholds that trigger a follow-up and any necessary intervention, then also considering data in conjunction with a planned internal review

- Formal staff feedback, which can involve periodic and/or end-of-engagement surveys or debriefs, or 360-degree feedback from reviewers, senior leaders, peers and staff members

- Client feedback, which includes an Audit Committee meeting on completion of the engagement and client surveys

- Unsolicited feedback from staff members, clients or other stakeholders

- A quality event, such as an audit client restatement or Australian Securities Exchange query.

Assessments need to be based on audit quality outcomes and behaviours that are measurable, consistent and transparent.

Measures of audit quality outcomes and behaviours will need to be developed to suit each network, firm or office, and they will be different for each role and firm. As roles, position titles and responsibilities vary between firms and jurisdictions, the categories used in this guide are indicative rather than definitive. Likewise, the measures of audit quality outcomes will vary considerably depending on the firm, the role of the individual and the data that can be captured with respect to audit quality outcomes and behaviours.

Assessments will need to ensure that measures are consistently applied so that the outcomes are comparable and transparent. While robustness and measurability are key in selecting measures, the measures should respond to changes in outcomes and the auditing environment, and would be expected to evolve over time. Furthermore, caution is needed in interpreting qualitative and quantitative measures, and understanding the interplay between measures. The conclusions that can be reasonably drawn from measures of audit quality and the responses that will be most effective must be identified using experience and judgement.

The audit quality outcomes and behaviours that a firm may seek to monitor, and examples of ways in which those outcomes and behaviours may be measured, are explored below. These examples are not definitive, they are provided to help firms develop measures that are useful in assessing audit quality for their audit leaders in a way that can be captured reliably.

A. Audit Practice Leader – assessment of audit quality outcomes and behaviours

The PL is responsible for the overall operation of the audit practice at the network, firm or office level, and oversees the performance of ELs and EQRs.

They should take actions necessary for the firm to meet its audit quality objectives, including:

- Establishing and maintaining a system of quality management that is designed appropriately and operates effectively

- Managing staffing and resourcing

- Providing adequate audit, assurance, technical accounting, industry or other engagement-appropriate resources, tools and training

- Supporting ELs and EQRs through coaching, reviews, and formal and informal feedback

- Providing an appropriate emphasis on quality and compliance processes, such as independence clearance, file management and mandatory training

- Setting an appropriate 'tone at the top'.

Below are examples of the ways in which a PL's audit quality outcomes and behaviours can be assessed.

(i) Quality outcomes relating to the review and inspection processes

The findings of internal reviews and external inspections of audit engagements (including observations and feedback), along with the PL's response to those findings, are key inputs when assessing a PL's performance. The findings themselves reflect the audit team's past quality outcomes, while the responses indicate whether shortcomings will be addressed in the current engagement and for future engagements. Whether targets for internal review and external inspection findings have been set and met should be considered.

The PL should be assessed for their responses in recognising exceptional findings and in ensuring poor findings are rectified, where possible, through remediation of methodology, practice management or other measures taken to improve future engagements. The PL is also responsible for ensuring that other audit leaders are recognised for exceptional review findings and held accountable for poor findings.

Where root cause analysis is undertaken to understand the causal factors for exceptional or poor audit review findings, the outcomes, as well as the PL's contribution and responses to the analysis, should also be taken into consideration when assessing their performance in relation to audit quality.

(ii) Quality behaviours

Measures should cover:

- Establishing and monitoring infrastructure and processes to support audit quality within a structured quality management system that addresses each of the elements of quality management

- Setting the right tone through actions such as:

  – Acting as a role model

  – Being actively engaged in all aspects of audit quality

  – Sharing best practices

  – Coaching the partner or leadership group

– Prioritising training

– Setting overall expectations

– Setting an appropriate tone on professional scepticism

– Undertaking active portfolio and resource management

The tone and commitment to audit quality may be assessed through EL and EQR feedback surveys, staff exit interviews, staff retention rates and the experience of staff members.

- Setting and communicating the vision and strategy for audit quality through actions such as:

  – Setting market priorities

  – Defining risk appetite

  – Investing in specialist, technical, educational and technological resources

- Engaging in the regulatory environment through actions such as:

  – Building strong relationships with key regulators

  – Participating in industry boards and committees

  – Setting out the firm's view of the regulatory agenda

  – Working with other audit leaders within the firm or network, or across firms, to improve or share best practices

- Driving strong quality processes, including owning and responding to assurance quality indicators, through actions such as:

  – Appropriately resourcing the audit practice

  – Reviewing client risk profiles

  – Reviewing EL portfolios to assess workloads and dependencies

  – Setting audit quality objectives

  – Implementing governance and monitoring against defined policies

  – Evaluating performance

  – Addressing quality and operational issues

  – Resolving disputes

  – Determining effective rewards and sanctions

  – Remediating quality issues swiftly

  – Successfully acting in assigned leadership roles.

B. Audit Engagement Leader – assessment of audit quality outcomes and behaviours

An EL is responsible for specific audit engagements and directly oversees engagement team members.

An EL's performance in relation to audit quality outcomes and behaviours under each component of quality management may be assessed in relation to:

- Governance and leadership, which includes:

  – Setting the 'tone at the top' – reinforcing quality, leading by example and 'walking the talk'

  – Mentoring staff and new audit leaders

  – Spending time on the job and with the client

  – The timing of EL involvement (not just the number of hours)

  – Being recognised for conducting complex, high-risk or challenging engagements

  – Contributing to the firm and the industry

  – Completing firm-required training

- Relevant ethical requirements, which includes:

  – Checking personal and team independence, and adequately addressing threats before commencing each engagement

  – Maintaining client confidentiality

- Acceptance and continuance of client relationships and engagements, which includes:

  – Ensuring that the EL, the team and experts have appropriate competencies, including industry knowledge, and are available

  – Accepting engagements only for which the firm has capacity

  – Ensuring that the client is suitable and meets the firm or office risk profile

- Resources, which includes:

  – Ensuring staffing and resources are sufficient to meet client needs and deliver a quality audit

  – Engaging internal or external specialist expertise, where appropriate

  – Facilitating and supporting staff training

  – Using the firm's tools and technical support

  – Ensuring team members receive continuous performance feedback

- Engagement performance, which includes ensuring that:

  – Engagement conduct meets auditing standards

  – Sufficient appropriate audit evidence is obtained

- Audit engagements are completed in a timely manner

- Team's technical knowledge is adequate for the engagement

- Professional judgements are made on a sound basis

- Sufficient time is spent on planning

- The EL spends sufficient time on each audit during the period

- Information and communication, which includes:

  - Managing file completion and archiving

  - Updating IT records

  - Ensuring documentation meets auditing standards, including providing sufficient appropriate audit evidence

  - Maintaining clear and constructive communication between client and team, including experts and the firm's technical team

- Monitoring and remediation, which includes:

  - Ensuring key professional judgements are reviewed, technical input is sought appropriately and differing views resolved

  - Reducing EL avoidance of engagements more likely to be subject to external review.

- Examples of measures to assess an EL's performance in relation to audit quality outcomes and behaviours are set out in Appendix 1.

C.   Engagement Quality Reviewer – assessment of audit quality outcomes and behaviours

An EQR is responsible for objectively evaluating the significant judgements the engagement team made and the conclusions the EL reached in formulating an opinion on a financial report. A firm's policies and procedures determine which engagements require an EQR, and small and medium-sized firms may resource the role externally.

The EQR should review key professional judgements and ensure any matters raised are resolved to their satisfaction, whether through the audit team obtaining further evidence, additional documentation, the use of experts, client adjustments, or the EL amending their auditor's report or management letter, if necessary.

Below are examples of the measures for assessing an EQR's audit quality outcomes and behaviours.

(i)   Quality outcomes relating to the review and inspection processes

The findings of internal reviews and external inspections, specifically those relating to judgements in the audit engagement, including observations and feedback communicated, are key inputs when assessing EQR performance. The EQR should be assessed on whether they adequately challenged the EL's key professional judgements and satisfactorily resolved issues raised prior to the auditor's report being signed.

(ii)   Quality behaviours

Measures should cover:

- Adequately challenging the EL's significant judgements and demonstrating professional scepticism during audit engagements

- Being involved in the engagement at key stages, including planning, reviewing significant judgements, sorting out difficult issues during the engagement and resolving matters before the auditor's report is signed off

- Challenging the appropriateness of the team's composition, including the use of internal or external experts

- Setting the right tone through actions such as:

    – Being a role model and sharing best practices

    – Coaching the EL or providing a sounding board

    – Demonstrating professional scepticism

    – Providing adequate and timely documentation to demonstrate that significant judgements and conclusions have been reviewed.

3.   Monitor Audit Quality Outcomes

Once appropriate audit quality outcomes and measures have been identified, they should be communicated to the PLs, ELs and EQRs who are to be assessed under the framework, before the relevant audits are undertaken.

Data on audit quality measures needs to be reliably captured to reflect audit quality outcomes and behaviours as a basis for assessing audit leaders. This provides credibility to the process for those being assessed and drives the desired audit quality behaviours. A process should be developed that translates the chosen audit quality outcomes into ratings as a basis for rewards and consequences for PLs, ELs and EQRs.

A mechanism for collating qualitative and quantitative data will be helpful in ensuring consistency and equity. Tools such as scoring models and the weighting of input data could also be considered so that 'hard data' (such as review outcomes) receives more prominence than 'soft' or anecdotal information. This could also incorporate consideration of a measure's significance and risk exposure.

Overall ratings

Developing a consistent rating scale is necessary to ensure there is no ambiguity regarding recognition and consequences. Ratings may be described differently by each firm, but would, at a minimum, involve four levels, such as:

1. Exceeds expectations

2. Meets expectations

3. Improvement required

4. Unsatisfactory

Examples of the basis for the rating assessment are set out in Appendix 2.

4. Implement Consequences and Rewards to Drive Audit Quality

Responses to audit quality behaviours and outcomes need to be transparent, consistent and fair, with the objective of reinforcing a culture that values audit quality and directly improves audit quality. As audit quality that 'meets expectations' is a requirement of the role for any audit leader, it should not attract additional public recognition or remuneration; however, 'exceeds expectations' indicates that more has been achieved than the role requires and should be recognised and/or rewarded.

The ways a firm can respond to an audit quality rating is outlined below.

A. Recognition

Recognition for audit quality performance that exceeds expectations may include:

- Incentives – increased remuneration, performance-related bonuses, salary raises and promotions

- Rewards – having success shared within the firm or publicly; getting opportunities to work on a choice of files, in a certain industry or location, or with a choice of staff; being given a mentoring or EQR role; becoming an advocate for the firm at the industry or regulatory level; being sent to selected conferences or courses; and receiving firm awards and/or acknowledgment at the office, firm or network level.

B. Accountability

Holding an individual accountable for performance that is unsatisfactory or requires improvement involves imposing consequences. The responses to accumulated 'unsatisfactory' or 'improvement required' ratings for audit quality outcomes depend on the materiality of each matter and the number of successive years an unsatisfactory rating has been achieved for that matter. Consequences may range from minor, such as additional training, to significant, such as removing the individual from the engagement. Responses may also take the form of support and coaching, financial penalties or loss of non-financial privileges. This includes:

- Penalties – remuneration is reduced, or all or part of a performance-related bonus is forfeited

- Remedial actions – includes development of a rectification plan which depends on the rating, the number of consecutive poor ratings, the severity of the negative findings and the risk to the firm and may include:

  – Less severe actions – requiring the individual to undergo training; offering greater support through shadowing or mentoring; imposing closer scrutiny; or removing the right to choose preferred engagements, staff or locations

  – More severe actions – limiting the nature (risk and complexity) of audits or types of industries or entities (e.g. no listed entities) which the individual can work on; requiring shadowing or mentoring on future engagements; undertaking a follow-up review within 12 months; taking the individual off audit engagements

Examples of recognition and accountability a firm may implement in response to ratings for PLs, ELs and EQRs are provided in Appendix 3.

5. Monitor and Review the Effectiveness of the Recognition and Accountability Framework

Firms should periodically consider the effectiveness of the framework to maintain or improve audit quality outcomes and to motivate quality behaviours. The indicators and measures of audit quality used to assess outcomes and behaviours and the nature of the recognition and accountability mechanisms implemented may need to be adjusted over time to remain effective. The audit environment changes over time and different factors become more important in maintaining audit quality. In addition, if audit leaders become too familiar with the measures being monitored, they may become complacent.

No one measure is infallible in assessing quality outcomes or behaviours, and each one needs to be considered in light of other measures and circumstances so that its relevance is not misinterpreted. Nevertheless, consistent measures enable comparison between periods and create greater certainty for the audit leaders being assessed. In contrast, constant change creates a greater administrative burden and may be demotivating if the goal posts are seen to be endlessly moving.

Benchmarking indicators and measures and considering root causes of exceptional and poor audit quality may be helpful ways to identify new, or eliminate existing, indicators and measures of audit quality outcomes and behaviours.

An effective recognition and accountability framework responds to the environment within the firm and the individuals being assessed. It also does not create an overly burdensome administrative process that may direct focus away from conducting quality audits. The data captured is not an end in itself and should not drive behaviours that may undermine audit quality. Indicators and measures need to be considered in context, not in isolation; otherwise, incorrect conclusions may be drawn or unintended consequences may arise.

Appendix 1 Examples of Audit Quality Measures for Engagement Leaders

Examples of measures to assess EL performance in relation to audit quality outcomes and behaviours are set out in the table below.

Component of audit quality	Audit quality outcome or behaviour	Example of audit quality measure
Governance and leadership	• Setting 'the tone at the top' – reinforcing quality, leading by example and 'walking the talk'	• Staff survey results – encouraging questioning, providing extra time when needed and not allowing individuals to cut corners • Retention of high performers • Exit interviews
	• Mentoring staff and new audit leaders	• Staff survey – extent and effectiveness of mentoring provided to senior members of audit team, and time spent with audit teams • 360-degree feedback
	• Spending time on the job and with the client • The timing of EL involvement (not just the number of hours)	• EL total hours and timing of hours on the job • Frequency of EL meetings with the client
	• Being recognised for conducting complex, high-risk or challenging engagements	• Annual portfolio assessment by partner • Proportion of engagements that are high profile or high risk – percentage of hours spent on clients or engagements with a high risk rating • Proportion of engagements that are challenging –percentage of clients that submit financial statements late; percentage of clients with going concern emphasis of matter or qualifications
	• Contributing to the firm and industry	• Hours providing formal staff training, or undertaking client training or industry presentations • Participation in industry discussion groups, external stakeholder groups or industry leadership roles • Development of new audit techniques or benchmarks • Participation in trialling new techniques, processes or IT tools
	• Completing firm-required training	• Extent to which EL has completed training • Extent to which team has completed training

Component of audit quality	Audit quality outcome or behaviour	Example of audit quality measure
Relevant ethical requirements	• Checking personal and team independence and adequately addressing threats before commencing each engagement	• Personal independence sign-off completed for each client and engagement • Team (including internal and external experts) independence sign-off completed for each client and engagement • Independence breaches identified • Independence threats identified and mitigated for each client
	• Maintaining client confidentiality	• Client confidentiality breaches reported
Acceptance and continuance of client relationships and engagements	• Ensuring that the EL, team and experts have appropriate competencies, including industry knowledge, and are available	• Staff survey – adequate expertise in the team to address issues arising, and adequate time to complete engagement • Internal review – EL and team possess relevant industry expertise or an expert is engaged
	• Accepting the firm's capacity for engagements	• Percentage of engagement deadlines met • Percentage of overtime hours worked by audit teams
	• Ensuring that the client is suitable and meets the firm or office risk profile	• Internal review – client risk assessed and considered acceptable • Client portfolio review
Resources	• Ensuring staffing and resources are sufficient to meet client needs and deliver a quality audit	• Internal review outcomes – appropriate number and level of staff members on team
	• Engaging specialist expertise, internal or external, where appropriate	• Internal review and staff survey – sufficient industry and technical expertise engaged or consulted
	• Facilitating and supporting staff training	• Staff survey – sufficient time allocated for training and no pressure to forfeit training; attendance at training prioritised, with EL leading by example • Training feedback form – training needs met
	• Using the firm's tools and technical support	• Internal review – firm's technical accounting or audit advisors consulted on complex audits • Staff survey – EL's willingness to consult and use available resources
	• Ensuring team members receive continuous performance feedback	• Staff survey – regular feedback on the job

Component of audit quality	Audit quality outcome or behaviour	Example of audit quality measure
Engagement performance	• Ensuring engagement conduct meets AUASB Standards	• Findings from internal reviews and external inspections (engagement rating)
	• Ensuring sufficient appropriate audit evidence is obtained	• Findings from internal reviews and external inspections[1]
	• Ensuring audit engagements are completed in a timely manner	• Percentage of engagements completed on time • Average number of days deadline exceeded by (caution is advised in interpreting this measure as it may reflect client tardiness or additional audit work needed to complete the engagement satisfactorily)
	• Ensuring technical knowledge is adequate for the engagement	• Findings from internal reviews and external inspections • Feedback from leaders supporting audit quality, including risk and quality; technical accounting and audit; independence compliance; and EQR • Extent of financial report technical review points
	• Ensuring professional judgements are made on a sound basis	• Findings from internal reviews and external inspections
	• Ensuring sufficient time is spent on planning	• Percentage of EL's time spent on planning
	• Ensuring the EL spends sufficient time on audits during the period	• Percentage of time EL spent on audits during the period
Information and communication	• Managing file completion and archiving	• Percentage completed within required timeframe after auditor's report was signed off
	• Updating IT records	• Percentage completed within required timeframe after auditor's report was signed off
	• Ensuring documentation meets auditing standards, including providing sufficient appropriate audit evidence	• Findings from internal reviews and external inspections (engagement rating)
	• Maintaining clear and constructive communication between client and team, including experts and firm's technical team	• Evaluation from internal review • Staff survey results • Feedback from EQR

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[1] Each individual PL, EL and EQR would normally be expected to be subject to an internal or external audit engagement review at least every three years; however, more frequent reviews may be necessary following a negative review.

Component of audit quality	Audit quality outcome or behaviour	Example of audit quality measure
Monitoring and remediation	• Ensuring key professional judgements are reviewed, technical input is sought appropriately and differing views resolved	• Findings from internal reviews and external inspections (engagement rating) • Clearance of EQR points and technical input • Appropriate response to external inspection findings to resolve or address issues for future engagements
	• Reducing EL avoidance of engagements more likely to be subject to external review	• Recognition if EL is the recipient of an external review (subject to satisfactory rating of externally reviewed files)

Appendix 2 Examples of the Basis for Rating Assessments

The following are some suggestions of the sorts of matters to consider when accumulating the detailed audit quality measures, to arrive at an overall rating. The basis for the rating assessment will also be affected by the experience of the individual being rated, as this will affect the expectations placed on them. For example, rating a newly promoted audit leader may involve focusing on the review and inspection findings rather than their contribution to audit quality improvements within the practice and may consider exceptional performance in less complex engagements, or having clients that are not as high risk as those handled by more senior audit leaders to be sufficient to achieve the 'exceeds expectations' rating.

A.   Practice Leader

Overall rating	Examples of basis of rating assessment
Exceeds expectations (exceptional)	• Two or more years of 'exceeds expectations' for the majority of the practice area for internal reviews and/or external inspections, where there have been no unsatisfactory file reviews • Consistently strong leadership and mentoring demonstrated, as assessed by ELs and staff • Contributed to the firm's audit quality by setting the tone for audit quality, demonstrated leadership through staff training, client training and contributing to industry thought leadership • Achieved tangible audit quality improvements in the practice area and/or across network through new or innovative programs
Meets expectations	• Two or more years of 'meets expectations' for the majority of the practice area for internal reviews and/or external inspections, where there have been no significant negative file reviews • Consistent or improved review findings • Audit quality not compromised despite internal or external pressures
Improvement required	• First year of 'unsatisfactory' rating for internal reviews and/or external inspections, with improvements identified • Deterioration in review findings
Unsatisfactory	• Negative internal reviews and/or external inspections of a significant nature • Negative internal reviews or external inspections of a less significant nature over two or more years • Independence breaches (statutory or regulatory requirements) • Required training not completed by PL and audit practice • Reputational damage to the firm or network

B.   Engagement Leader

C.   Engagement Quality Reviewer

Overall rating	Examples of basis of assessment
Exceeds expectations (exceptional)	- Two or more years of 'exceeds expectations' for internal reviews and/or external inspections - No negative file reviews - Consistently strong leadership and mentoring demonstrated, as assessed by peers and staff - Contributed to the firm's audit quality by acting as an EQR, providing staff and client training, and contributing to industry thought leadership - Exceptional technical skills and judgement observed by quality and risk team, financial reporting technical team and other peers - Strong record of effectively handling complex engagements or high-risk clients
Meets expectations	- Two or more years of 'meets expectations' for internal reviews and/or external inspections - No negative file reviews - Audit quality not compromised despite internal or external pressures - Satisfactory leadership and mentoring demonstrated, as assessed by peers and staff
Improvement required	First year of negative internal reviews and/or external inspections of a less significant nature
Unsatisfactory	- Negative internal reviews and/or external inspections of a significant nature - Negative internal reviews and/or external inspections of a less significant nature over two or more years - Independence breaches (statutory or regulatory requirements) - Required training not completed - Reputational damage to the firm or network

Appendix 3 Examples of Recognition and Accountability

The following tables outline how the above examples of consequences or recognition might apply to the audit leadership roles for the different rating levels.

A.   Audit Practice Leader

Overall rating	Examples of recognition (incentives and rewards) and accountability (consequences)
Exceeds expectations (exceptional)	• Acknowledgement across the firm and network, via newsletter, presentation or award • 'Exceeds expectation' rating for audit quality has a positive impact on the overall performance rating for performance-based remuneration
Meets expectations	• Recognised at the firm level • Training and mentoring offered to target exceptional performance
Improvement required	• Review meeting with a member of the firm's leadership • Remediation plan developed, incorporating outcomes of root cause analysis • Specific leadership training and ongoing coaching provided • Support provided to address shortcomings, such as technical resources, additional time or staff • 'Improvement required' rating for audit quality has a negative impact on the overall performance rating for performance-based remuneration
Unsatisfactory	• Review meeting with senior leadership • Remediation plan developed, incorporating outcomes of root cause analysis • Specific leadership training and ongoing coaching provided • Support – such as technical resources, additional time or staff – provided to the practice area to address shortcomings • Triggers practice review and independence review • 'Unsatisfactory' rating for audit quality has a significantly negative impact on the overall performance rating for performance-based remuneration • Removal from leadership role and audit practice may be considered.

B.   Engagement Leader

C.   Engagement Quality Reviewer

Overall rating	Examples of recognition (rewards) and accountability (consequences)
Exceeds expectations (exceptional)	• Recognised across the firm • Exceptional rating for audit quality has a positive impact on the overall performance rating for performance-based remuneration
Meets expectations	• Recognised at the local audit practice level • Training and mentoring offered to target exceptional performance
Improvement required	• Annual review meeting with PL • Remediation plan developed, incorporating outcomes of root cause analysis • Specific targeted training, ongoing coaching or mentoring provided • Support – such as technical resources, additional time or staff – provided to engagements to address shortcomings • Client portfolio or role as an EQR reviewed • 'Improvement required' rating for audit quality has a negative impact on the overall performance rating for performance-based remuneration • Files selected for further review • Reviewed more frequently
Unsatisfactory	• Annual review meeting with PL and a member of the leadership team • Remediation plan developed, incorporating outcomes of root cause analysis • Specific targeted training and ongoing coaching provided • Support, such as technical resources, additional time or staff, provided to engagements to address shortcomings • Client portfolio reviewed, including no listed entities, public interest entities or industries where EL has insufficient expertise and role as an EQR reviewed • 'Improvement required' rating for audit quality has a very negative impact on the overall performance rating for performance-based remuneration • Mentor appointed for future engagements • Files selected for further review • Reviewed more frequently in the future • Transfer out of the audit practice considered • Approval to perform (certain) audits removed

Contacts and request for feedback

This guide was developed by CPA Australia on behalf of the APPC. It is aimed to be a useful tool for firms of any size and as such we welcome feedback from small and medium sized firms on how the guide could be improved or made more relevant to you. It is based on the insights and experiences shared by representatives of the large networked firms while recognising the needs of different sized firms. CA ANZ and CPA Australia will be undertaking targeted consultation with members to incorporate feedback.

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