



Establishing and Maintaining a **System of Quality Management** for a CPA Firm's Accounting and Auditing Practice

Chapter 1: Overview of Statement
on Quality Management Standards No. 1

For Small- and
Medium-Sized Firms



Quality Management Implementation Task Force

Alan Long, *Chair*

Toby Akrab

Brian Bluhm

Sherry Chesser

Horace Emery

Katherine Fletcher

Greg Jenkins

Phil Laycock

Joseph Lynch

Richard W. Reeder

Mike Westervelt

AICPA Staff

Jennifer Burns, CPA

Chief Auditor

Professional Standards and Services

Ahava Z. Goldman, CPA

Associate Director

Audit and Attest Standards

Jennifer Gum, CPA

Manager — Audit Quality Initiatives

Audit and Accounting Quality

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This practice aid does not address the quality control requirements of the Sarbanes-Oxley Act of 2002 (SOX), nor does it address the quality control requirements of PCAOB standards that auditors of issuers must follow. Auditors of issuers should follow these other standards and make changes to their firm's quality control systems as necessary.

Additional information about the PCAOB and SOX can be obtained at the PCAOB website at pcaobus.org.

How to use this practice aid

This AICPA Audit and Accounting Practice Aid, *Establishing and Maintaining a System of Quality Management for a CPA Firm's Accounting and Auditing Practice*, is intended to help practitioners design, implement, and operate a system of quality management for their firm's accounting and auditing practice, as required by Statement on Quality Management Standards (SQMS) No. 1, *A Firm's System of Quality Management*, issued by the AICPA.

SQMS No. 1 requires the firm to apply a risk-based approach in designing, implementing, and operating the components of the system of quality management. In applying a risk-based approach, the firm is required to take into account the nature and circumstances of both the firm and the engagements performed by the firm. This practice aid explains how to apply a risk-based approach and includes a library of potential risks and suggested responses.

Use this practice aid, and the Example Risk Assessment template, to help you apply the risk-based approach, identify the quality risks to your practice, and implement policies and procedures as necessary for the facts and circumstances of your practice.

Many of the policies and procedures may need to be modified to be applicable to your firm. Some may not be applicable at all. You may need to add policies and procedures that are already part of your system. Some of the policies and procedures are required by SQMS No. 1; these are noted in chapters 3 and 4.

Be aware that if you do not customize the risks and responses to the nature of your practice

- you won't be in compliance with the standards.
- you won't be doing what is most efficient and effective for your practice.

If all you do is

- copy the quality risks from this practice aid, it is likely that your quality risks will be incomplete, or that you will include quality risks that do not apply to your firm. Do not copy the quality risks from this practice aid without thoughtful consideration of any modifications needed for your firm's nature and circumstances.
- copy and paste the policies and procedures in this practice aid, you will be committing to responses that may not apply to your firm. And, because you included them in your documentation of your system of quality management, your peer reviewer will expect you to apply those policies and procedures.

In addition, a firm's risk assessment should be iterative and updated when changes in the nature and circumstances of the firm or its engagements occur. An incomplete or out-of-date risk assessment can have a significant effect on the system of quality management.

This practice aid is intended for firms with two or more personnel. If your firm has only one assurance partner, or only one partner with expertise in a specialized area, you may find the AICPA Audit and Accounting Practice Aid *Establishing and Maintaining a System of Quality Management for a CPA Firm's Accounting and Auditing Practice* for sole practitioners, also helpful.

Chapter 1 – Overview of statements on quality management standards

Statement on Quality Management Standards (SQMS) No. 1, *A Firm's System of Quality Management*, (QM section 10),¹ was issued by the Auditing Standards Board of the AICPA in June 2022 and is effective for a firm's accounting and auditing practice as of December 15, 2025. This standard supersedes Statement on Quality Control Standards No. 8, *A Firm's System of Quality Control*.²

The biggest change reflected in the new QM standard is the introduction of a risk-based approach in designing, implementing, and operating a system of quality management (SOQM), which helps firms identify and address risks specific to their practice and creates a more scalable approach to quality for all firms. The risk-based approach comprises (a) establishing quality objectives (the desired outcomes relating to the components of the SOQM to be achieved by the firm); (b) identifying and assessing quality risks (a risk that has a reasonable possibility of occurring and, individually or in combination with other risks, adversely affecting the achievement of one or more quality objectives); and (c) designing and implementing responses (policies or procedures designed and implemented by the firm to address one or more quality risks).

The standard's approach emphasizes the responsibility of firm leadership for proactively managing quality and provides flexibility to deal with differences in the size of firms and the nature of the services they provide. The essence of this approach is to focus firms' attention on risks that may have an impact on engagement quality. The approach requires a firm to customize the design, implementation, and operation of its SOQM based on the nature and circumstances of the firm and the engagements it performs. The standard also has an increased emphasis on a continual flow of remediation and improvement.

An SOQM addresses the following eight components, which are highly integrated and do not act in a linear manner:

1. The firm's risk assessment process
2. Governance and leadership
3. Relevant ethical requirements
4. Acceptance and continuance of client relationships and specific engagements
5. Engagement performance
6. Resources
7. Information and communication
8. The monitoring and remediation process

The objective of the firm is to design, implement, and operate an SOQM for its accounting and auditing practice that provides the firm with reasonable assurance that

- the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements and conduct engagements in accordance with such standards and requirements, and
- engagement reports issued by the firm are appropriate in the circumstances.

In this context, reasonable assurance is not intended to be obtained through independent assurance that the system is effective (for example, by having a peer review every year); instead, it is obtained through the operation of the system as a whole.

¹ The QM sections can be found in AICPA *Professional Standards*.

² The Statements on Quality Control Standards are codified in the QC sections in AICPA *Professional Standards*.

The firm's risk assessment process

The purpose of the risk assessment process element of an SOQM is to establish quality objectives, identify and assess quality risks, and design and implement responses to address the quality risks. The risk assessment process section of SQMS No. 1 focuses firms' attention on risks that may have an impact on engagement quality.

The risk assessment is a three-step process:

1. **Establish quality objectives.** The standard requires the firm to establish specific quality objectives for each component except risk assessment and monitoring and remediation. The firm is required to establish additional quality objectives when necessary to achieve the objective of the SOQM. However, the firm may not find it necessary to establish additional quality objectives.
2. **Identify and assess risks to the achievement of the quality objectives** (referred to in the standard as quality risks). Identifying and assessing quality risks involves
 - a. understanding the factors (that is, the conditions, events, circumstances, actions, or inactions) that may adversely affect the achievement of the quality objectives and

- b. taking into account how and the degree to which the factors may adversely affect the achievement of the quality objectives. (The assessment of identified quality risks does not require formal ratings or scores.)

A risk arises from how, and the degree to which, a condition, event, circumstance, action, or inaction may adversely affect the achievement of a quality objective. Not all risks meet the definition of a quality risk.

3. **Design and implement responses to address the quality risks.** The nature, timing, and extent of the firm's responses to address the quality risks are based on, and responsive to, the reasons for the assessments given to the quality risks. Certain responses are specified in the standard; however, the specific responses required by the standard will not be sufficient for the firm to address all its quality risks.

Firms are also required to identify information indicating the need for additions or modifications to quality objectives, quality risks, or responses.

Governance and leadership

The purpose of the governance and leadership element of an SOQM is to promote an internal culture based on the recognition that quality is essential in performing engagements. The governance and leadership section of SQMS No. 1 addresses the expected behavior of firm leadership in setting the tone at the top, the appropriate qualifications of leadership, and holding leadership accountable through performance evaluations. The standard also addresses the importance of quality in the firm's strategic decisions and actions — including financial and operational priorities — as well as firm leadership's ability to influence decisions about the firm's resources.

The firm is required to assign ultimate responsibility and accountability for the SOQM to the firm's CEO, managing partner (or equivalent), or if appropriate, managing board of partners (or equivalent).

In addition, the firm is required to assign the following to designated individuals:

- Operational responsibility for the SOQM
- Operational responsibility for specific aspects of the SOQM, including compliance with independence requirements and the monitoring and remediation process

SQMS No. 1 emphasizes the firm's commitment to quality through a culture that reflects the firm's role in serving the public interest through consistent quality engagements. Leadership demonstrating a commitment to quality through its actions and behaviors reinforces the responsibility that all personnel hold for quality relating to the performance of engagements and activities within the SOQM.

Relevant ethical requirements

The purpose of the relevant ethical requirements element of an SOQM is to provide the firm with reasonable assurance that the firm and its personnel comply with relevant ethical requirements when performing professional responsibilities. The relevant ethical requirements component of SQMS No. 1 addresses responsibilities regarding ethical requirements for the firm and its personnel as well as others in the firm's network. The following quality objectives should be established relating to the firm and its personnel:

- Understand the relevant ethical requirements to which the firm and the firm's engagements are subject.
- Fulfill their responsibilities in relation to the relevant ethical requirements to which the firm and the firm's engagements are subject.

The firm should also ascertain that others (including the network, network firms, individuals in the network or network firms, or service providers) who are subject to the relevant ethical requirements to which the firm and the firm's engagements are subject

- understand the relevant ethical requirements that apply to them, and
- fulfill their responsibilities in relation to the relevant ethical requirements that apply to them

Examples of relationships between the relevant ethical requirements component and other components include the following:

- The information and communication component may address the communication of various matters related to relevant ethical requirements, including
 - the firm communicating the independence requirements to all personnel and others subject to independence requirements.
 - personnel and engagement teams communicating relevant information to the firm without fear of reprisals, such as situations that may create threats to independence or breaches of relevant ethical requirements.
- As part of the resources component, the firm may
 - assign individuals to manage and monitor compliance with relevant ethical requirements or to provide consultation on matters related to relevant ethical requirements.
 - use IT applications to monitor compliance with relevant ethical requirements, including recording and maintaining information about independence.

The relevant ethical requirements that apply to others depend on the provisions of the relevant ethical requirements and how the firm uses others in its SOQM or in performing engagements. Examples follow:

- Relevant ethical requirements may include requirements for independence that apply to network firms or employees of network firms.
- The principle of confidentiality may apply to the firm's network, other network firms, or service providers when they have access to client information obtained by the firm.

Acceptance and continuance of client relationships and specific engagements

The purpose of the acceptance and continuance of client relationships and specific engagements component of an SOQM is to provide reasonable assurance that the firm makes appropriate judgments about whether to accept or continue a client relationship and whether to perform a specific engagement. A firm's acceptance and continuance policies represent a key element in quality management, while also mitigating litigation and business risk. This component of SQMS No. 1 also addresses quality objectives for firms around client acceptance and continuance decisions. These objectives include judgments by the firm to accept or continue a client relationship or specific engagement based on

- information obtained about the nature and circumstances of the engagement.

- information obtained about the integrity and ethical values of the client, including the identity and business reputation of the client's principal owners, key management, and those charged with its governance.
- the firm's ability to perform the engagement in accordance with professional standards, and applicable legal and regulatory requirements

SQMS No. 1 also emphasizes that the financial and operational priorities of the firm should not lead to inappropriate judgments about whether to accept or continue a client relationship or specific engagement.

Engagement performance

The purpose of the engagement performance element of an SOQM is to provide the firm with reasonable assurance that engagements are consistently performed in accordance with applicable professional standards and regulatory and legal requirements and that the firm issues reports that are appropriate in the circumstances. The engagement performance section of SQMS No. 1 provides quality objectives that firms should establish to obtain reasonable assurance that high-quality performance is being attained in the firm's engagements. Establishing and maintaining quality objectives such as the following help the firm in obtaining reasonable assurance relating to the engagement performance element of an SOQM:

- Engagement teams understand and fulfill their responsibilities in connection with the engagements, including, as applicable, the overall responsibility of engagement partners for managing and achieving quality on the engagement and being sufficiently and appropriately involved throughout the engagement.
- The nature, timing, and extent of direction and supervision of engagement teams and review of the work performed is appropriate based on the nature and circumstances of the engagements and the resources

assigned or made available to the engagement teams; the work performed by less experienced engagement team members is directed, supervised, and reviewed by suitably experienced engagement team members.

- Engagement teams exercise appropriate professional judgment and, when applicable to the type of engagement, maintain professional skepticism.
- Consultation on difficult or contentious matters is undertaken, and the conclusions agreed to are implemented.
- Differences of opinion within the engagement team, or between the engagement team and the engagement quality reviewer or individuals performing activities within the firm's SOQM, are brought to the attention of the firm and resolved.
- Engagement documentation is assembled on a timely basis after the date of the engagement report and is appropriately maintained and retained to meet the needs of the firm and comply with law, regulation, relevant ethical requirements, and professional standards.

Resources

The purpose of the resources element of an SOQM is to provide the firm with reasonable assurance that it is appropriately obtaining, developing, using, maintaining, allocating, and assigning resources in a timely manner to enable the design, implementation, and operation of the SOQM. SQMS No. 1 addresses all resources that the firm needs both to operate the system and to perform engagements. These resources cover the following:

- **Technological resources.** For example, audit tools or IT applications used by the firm for independence monitoring.
- **Intellectual resources.** For example, the firm's methodology, guidance, templates, or tools.
- **Human resources.** This may include people outside the firm used in engagements, including component auditors or engagement quality reviewers who are external to the firm.

The standard focuses on what resources are needed, how they are used and maintained, and whether they are appropriate. The principles-based nature of the requirements relating to resources takes into account the variety of resources used and their source. The resources section of SQMS No. 1 also covers the use of resources from service providers and how to determine that those resources are appropriate for the intended use by the firm. A resource from a service provider could be a methodology, an IT application, or people used in an engagement. Services that come from a firm's network, if the firm belongs to a network, are not considered as coming from a service provider.

Information and communication

The purpose of the information and communication element of an SOQM is to address the importance of communicating information obtained, generated, or used both within the firm and to external parties on a timely basis to enable the design, implementation, and operation of the SOQM.

This component of SQMS No. 1 underscores the importance of a continuous flow of information and communication by linking the exchange of information to the firm's culture so that it is driven from top leadership throughout the firm. The standard requires that the firm establish an information system with processes to identify, capture, process, and maintain information, acknowledging that less complex firms with fewer personnel and direct involvement of leadership may

accomplish the objective with less rigorous or detailed policies and procedures.

This component of SQMS No. 1 also encourages firms to be transparent to external parties about their SOQM in a relevant, innovative, and proactive manner. This component requires that firms establish policies and procedures that address when communications with external parties are appropriate. To promote continual innovation in this area, the standard provides flexibility regarding the specific information communicated, the form of that communication, and the nature, timing, and extent of communication.

Monitoring and remediation

The purpose of the monitoring and remediation process element of an SOQM is to provide the firm with relevant, reliable, and timely information about the design, implementation, and operation of the SOQM so the firm may take appropriate action to remediate identified deficiencies on a timely basis. SQMS No. 1 focuses on monitoring activities that address the entire SOQM. The standard emphasizes performing tailored monitoring activities sufficient to provide a basis for the firm to evaluate the SOQM.

The requirements also emphasize factors that firms should consider in designing monitoring activities, rather than prescribing such activities. The nature, timing, and extent of monitoring activities will be driven by many firm-specific factors including the following:

- How the underlying system is designed
- The nature and circumstances of the firm and engagements it performs
- The extent of changes to the system
- The results of previous monitoring activities or external inspections

This component includes a requirement to inspect completed engagements and for engagement partners to be inspected on a cyclical basis. The firm determines its inspection criteria, including how often to select completed engagements, which completed engagements to select, which engagement partners to select, and how frequently to select an engagement partner. In doing so, the firm takes into account factors such as other types of monitoring the firm does, areas of risk, and how the system is designed.

The standard includes requirements for evaluating findings, identifying deficiencies, and evaluating the severity and persuasiveness of the deficiencies. These include a requirement to investigate the root cause of identified deficiencies. The requirement is intended to be flexible to encourage firms to scale the nature, timing, and extent of the procedures to investigate the root cause of the deficiencies so that they are appropriate and tailored to the circumstances. The evaluation of the severity and pervasiveness of deficiencies is also used by leadership in evaluating the system and concluding whether it achieved its objectives.



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