



**Meeting:** IAASB Consultative Advisory Group (CAG)

**Meeting Location:** Virtual Zoom Meeting

**Meeting Date:** September 8–9, 2020

## Agenda Item B1

### Proposed ISQM 1<sup>1</sup> – Cover and Report Back

#### Objectives of Agenda Item

1. The objectives of this agenda item are to:
  - (a) Provide a report back on comments of the Representatives on this project as discussed at the March 2020 meeting (see Appendix C).
  - (b) Obtain Representatives' views on the ISQM 1 Task Force's (TF) proposals on external communications and how the standard addresses the public interest and how it is related to the objective of the standard.

#### Project Status and Timeline

2. At the March 2020 CAG meeting, the ISQM 1 TF Chair presented respondents' feedback on the remaining areas that were not discussed previously with the CAG. At the time, the intention was to approve the standard in June 2020. However, given the impact of COVID-19 on the IAASB's work plan and its stakeholder's capacity, the approval of proposed ISQM 1 was deferred to September 2020.
3. The ISQM 1 TF and the IAASB are working towards approval of the final standard, and its related conforming and consequential amendments, in September 2020.
4. Appendix A to this paper provides a history of previous discussions with the IAASB CAG and the IAASB on this topic, including links to the relevant IAASB CAG documentation.

#### *IAASB Interaction with the IAASB CAG with Respect to Proposed ISQM 1*

5. The substantive issues being raised for the purposes of the September 2020 IAASB meeting are highlighted in this paper and have been summarized in **Agenda Item B1.1**. Accordingly, this serves as the final discussion of ISQM 1 before its anticipated approval by the IAASB in September 2020.
6. Representatives and Observers may wish to take this opportunity to comment on the IAASB's interaction with the CAG during the development and finalization of ISQM 1.

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<sup>1</sup> Proposed International Standard on Quality Management (ISQM) 1 (Previously International Standard on Quality Control 1), *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

## CAG Discussion in September 2020

7. **Agenda Item B1.2** is the clean version of proposed ISQM 1 that will be discussed by the IAASB at the upcoming September 2020 meeting. The revisions to proposed ISQM 1 since the previous discussion with the CAG include changes discussed with, or to be presented to, the IAASB as follows:
- (a) The changes discussed with the IAASB on April 8, 2020 (this formed part of a turnaround of the standard as part of the March 2020 meeting).
  - (b) The changes discussed with the IAASB in June 2020, which focused on key areas of proposed ISQM 1. The goal of the discussion was to achieve consensus on these key areas to facilitate the approval of the standard in September 2020.
  - (c) The proposed changes that will be discussed with the IAASB in September 2020.
8. The table below highlights the key changes made since the last discussion with the CAG, and includes references to the relevant sections of the IAASB papers explaining these changes. **Agenda Item B1.1** also summarizes the reasons for, and the nature of the changes. For the purposes of the CAG discussion, the ISQM 1 TF Chair will present the ISQM 1 TF's proposals on these changes (see **Agenda item B1.1**). Representatives will then be asked to provide input on the questions outlined below in this paper.

Areas of key change	IAASB Papers
Introductory material addressing the public interest was relocated to the objective of the standard	<ul style="list-style-type: none"><li>• <b>Section B.2</b> of <a href="#">Agenda Item 2</a> of the IAASB September 2020 meeting</li></ul>
Further enhancements were made to address external communications	<ul style="list-style-type: none"><li>• Paragraphs 40(d), 41A(dA), A145–A153, A153GA–A153GD of <a href="#">Agenda Item 4–A (Updated)</a> of the IAASB April 2020 meeting</li><li>• <a href="#">Agenda Item 5-D</a> of the IAASB June 2020 meeting</li><li>• <b>Section B.5</b> of <a href="#">Agenda Item 2</a> of the IAASB September 2020 meeting</li></ul>

9. Since the last discussion with the CAG, the ISQM 1 TF also considered various matters related to human resources used in performing engagements, and coordinated with the ISA 220<sup>2</sup> TF and ISA 600<sup>3</sup> TF. This resulted in revisions to proposed ISQM 1 to clarify the firm's responsibilities related to human resources used in performing engagements. These revisions were technical in nature and focused on clarifying the intent of the standard. As a result, they have not been identified as a key change for the CAG. However, for reference, the IAASB papers explaining the revisions are as follows:

<sup>2</sup> Proposed ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

<sup>3</sup> ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

- (a) **Section B.6** of [Agenda Item 5](#) of the IAASB June 2020 meeting; and
  - (b) **Section B.1** of [Agenda Item 2](#) of the IAASB September 2020 meeting.
10. In referring to the IAASB papers highlighted above, please note:
- (a) The questions in the IAASB papers, including those in **Agenda Item 2** of the IAASB September 2020 meeting, are those that have been, or will be, posed to the IAASB. Therefore, Representatives are not being asked to respond to these questions. The **Matters for IAASB CAG Consideration** are outlined below.
  - (b) [Agenda Item 2](#) of the IAASB September 2020 meeting includes references to a variety of other agenda items that will be presented at the September 2020 IAASB meeting. These agenda items have not been referenced or provided for the purposes of the IAASB CAG discussion, but are available at <https://www.iaasb.org/meetings/iaasb-board-meeting-virtual-videoconferencing-1>.

*Other Appendices to this Paper*

- 11. **Appendix B** to this paper provides a list of outreach between March 2020 and August 2020 regarding proposed ISQM 1.
- 12. **Appendix C** to this paper presents a report-back on the matters discussed with the CAG at the March 2020 meeting.

**Matters for IAASB CAG Consideration**

- 1. Do Representatives support the position of the paragraph explaining the public interest and how it is related to the objective of the standard (paragraph 15 of **Agenda Item B1.2**)?
- 2. Do Representatives believe that the proposed enhancements to the requirement addressing external communications (paragraph 34(e) of **Agenda Item B1.2**) and related application material (paragraphs A124–A132 of **Agenda Item B1.2**) are appropriate?
- 3. Representatives are asked whether there are any other matters that should be considered by the IAASB before finalizing proposed ISQM 1?

**Material Presented – IAASB CAG Papers**

<b>Agenda Item B1.1</b>	Presentation – Proposed ISQM 1
<b>Agenda Item B1.2</b>	Draft of Proposed ISQM 1 (Clean)

**Material Presented – IAASB CAG Reference Papers**

<a href="#">Agenda Item 4–A (Updated)</a> of the IAASB April 2020 meeting	Draft of Proposed ISQM 1 (Track Changes from Agenda Item 4–A of the March 2020 Meeting)
<a href="#">Agenda Item 5–D</a> of the IAASB June 2020 meeting	Proposed ISQM 1: External Communications – Additional Proposals for Consideration by the Board
<a href="#">Agenda Item 2</a> of the IAASB September 2020 meeting	Proposed ISQM 1: Issues and Recommendation

## Appendix A

### Project History

Project: [ISQM 1](#)

#### Summary

	IAASB CAG Meeting	IAASB Meeting
Project Commencement	March 2015 September 2015 September 2016	June 2014 (Quality Control only) December 2014 March 2015 June 2015 September 2015 December 2015 June 2016 September 2016
Project proposal	November 2016 Teleconference	December 2016
ISQC 1 issues discussion, including ISQC 2 addressing EQC reviews	March 2017 September 2017	December 2016 March 2017 June 2017 August 2017 September 2017
First Read of Draft Exposure Draft of Proposed ISQC 1		December 2017
Second Read of Draft Exposure Draft of Proposed ISQC 1	March 2018	March 2018
Third Read of Draft Exposure Draft of Proposed ISQC 1	September 2018	September 2018
Exposure Draft of ISQM 1 approved	March 2019 (Update and report back)	December 2018
Development of Final Standard	September 2019	September 2019

	March 2020	December 20219 March 2020 April 2020 June 2020
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### **IAASB CAG Discussions: Detailed References**

Information Gathering: Responding to Calls to Enhance Audit Quality	<p><u>March 2015</u></p> <p>See IAASB CAG meeting material and CAG meeting minutes (Agenda Item B and C).</p> <p><a href="http://www.ifac.org/meetings/new-york-usa-5">http://www.ifac.org/meetings/new-york-usa-5</a></p> <p><u>September 2015</u></p> <p>See IAASB CAG meeting material and CAG meeting minutes (Agenda Item F).</p> <p><a href="http://www.iaasb.org/cag/meetings/new-york-usa-0">http://www.iaasb.org/cag/meetings/new-york-usa-0</a></p>
Information gathering: Overview of Responses to the ITC, Group Audits and Engagement Quality Control Reviews	<p><u>September 2016</u></p> <p>See IAASB CAG meeting material and CAG meeting minutes (Agenda Item G).</p> <p><a href="http://www.iaasb.org/cag/meetings/new-york-usa">http://www.iaasb.org/cag/meetings/new-york-usa</a></p>
Project Proposal	<p><u>November 2016</u></p> <p>See IAASB CAG meeting material and CAG meeting minutes (Agenda Item B).</p> <p><a href="http://www.iaasb.org/cag/meetings/iaasb-cag-conference-call-november-29-2016-730-am-1030-am-est">http://www.iaasb.org/cag/meetings/iaasb-cag-conference-call-november-29-2016-730-am-1030-am-est</a></p>
ISQC 1 Issues Discussion, Including EQC Reviews	<p><u>March 2017</u></p> <p>See IAASB CAG meeting material and CAG meeting minutes (Agenda Item H).</p> <p><a href="http://www.iaasb.org/cag/meetings/iaasb-cag-meeting">http://www.iaasb.org/cag/meetings/iaasb-cag-meeting</a></p> <p><u>September 2017</u></p> <p>See IAASB CAG meeting material and CAG meeting minutes (Agenda Item D).</p> <p><a href="http://www.iaasb.org/cag/meetings/iaasb-cag-meeting-madrid-spain">http://www.iaasb.org/cag/meetings/iaasb-cag-meeting-madrid-spain</a></p> <p><u>March 2018</u></p> <p>See IAASB CAG meeting material and CAG meeting minutes (Agenda Item D).</p> <p><a href="http://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny">http://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny</a></p> <p><u>September 2018</u></p> <p>See IAASB CAG meeting material and CAG meeting minutes (Agenda Item C).</p>

	<a href="https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny-0">https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny-0</a>
ISQM 1 Update and Report Back	<u>March 2019</u> See IAASB CAG meeting material and CAG meeting minutes (Agenda Item H). <a href="https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny-1">https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny-1</a>
ISQM 1 Development of Final Standard	<u>September 2019</u> See IAASB CAG meeting material and CAG meeting minutes (Agenda Item C) <a href="https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny-2">https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny-2</a> <u>March 2020</u> See IAASB CAG meeting material and CAG meeting minutes (Agenda Item B) <a href="https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny-3">https://www.iaasb.org/cag/meetings/iaasb-cag-meeting-new-york-ny-3</a>

## Appendix B

### Outreach

1. Various outreach activities took place between March 2020 and August 2020, that had a particular focus on proposed ISQM 1. These outreach activities included:
  - A presentation to, and discussion with, the IFAC Small and Medium Practices Committee;
  - A presentation and panel discussion with the Forum of Firms and Global Public Policy Committee;
  - A presentation to national audit standards setters about the effective date of the proposed standard;
  - A presentation and roundtable discussion with the Global Public Policy Committee on the effect of COVID-19 on implementation efforts;
  - A presentation to Crowe Global – Americas Region; and
  - A presentation to, and discussion with, the International Forum of Independent Audit Regulators Standards Coordination Working Group and Global Audit Quality Working Group.

## Appendix C

### Report-Back on Matters Discussed at the March 2020 CAG Meeting

Extracts from the draft minutes of the March 2020 IAASB CAG meeting, as well as an indication of how the ISQM 1 TF or IAASB has responded to the Representatives' comments, are included in the table below.

Representatives' Comments	ISQM 1 TF/IAASB Response
THE FIRM'S RISK ASSESSMENT PROCESS AND THE APPROACH TO QUALITY OBJECTIVES AND RESPONSES	
Mr. Dalkin enquired about the impact of proposed ISQM 1 on a small firm and how such firms would demonstrate compliance with proposed ISQM 1.	Ms. Corden emphasized that proposed ISQM 1 will be a change for firms. Ms. Corden further explained that how a firm achieves the quality objectives may vary, and the collective achievement of the quality objectives would result in the achievement of the overall objective of the standard. She added that the risk factors in the standard are intended to assist firms in thinking about the risks to achieving the quality objectives, and are focused on the nature and circumstances of the firm to drive a mindset that is focused on scaling the system to be suitable for the firm's circumstances. However, she emphasized that there is not a requirement for firms to demonstrate that they have considered every risk factor in proposed ISQM 1 for every quality objective and document a complex matrix that evidences that they have done so. Ms. Corden explained that in a simpler firm, there may be fewer and less concise quality risks, as the standard allows firms to scale down the system to their nature and circumstances, while still maintaining a robust system. Ms. Corden added that more complex firms may need a more elaborate risk assessment process. Mr. Dalkin emphasized the importance of education and communication to smaller firms to clarify the intent that firms are not expected to address the risk factors as a checklist. Ms. Corden highlighted that outreach will be taking place with the IFAC SMP Committee prior to the March 2020 IAASB meeting.



Representatives' Comments	ISQM 1 TF/IAASB Response
<p>Ms. Zietsman highlighted the importance of proposed ISQM 1 to the Public Company Accounting Oversight Board (PCAOB), given the recent PCAOB Quality Control Concept Release. Ms. Zietsman emphasized her support for the approach in the firm's risk assessment process. She emphasized that the factors provide a good structure and are important in driving scalability upwards and downwards, although indicated the need to demonstrate how they will operate for less complex firms.</p>	<p>Support Noted.</p>
<p>Mr. Hirai indicated his support for the term "quality risk considerations" and defining the term, because it is more consistent with the recently approved ISA 315 (Revised 2019)<sup>4</sup> and could drive more proactivity in identifying and assessing quality risks.</p>	<p>Support noted.</p> <p>Ms. Corden indicated that in the December 2019 IAASB meeting, the IAASB supported the principle of introducing quality risk considerations and aligning concepts with ISA 315 (Revised 2019), but the IAASB had encouraged the ISQM 1 TF to consider whether the term "quality risk considerations" is the most appropriate term, and whether the definition of the term is needed.</p> <p>The IAASB has subsequently agreed to changing the quality risk considerations to conditions, events, circumstances, actions or inactions that may adversely affect the achievement of the firm's quality objectives, which is conceptually aligned with the concept in the definition of business risk in ISA 315 (Revised 2019).</p>
<p>Mr. Ruthman suggested that the risk factor in paragraph 22E(a)(i)(c)<sup>5</sup> of proposed ISQM 1, which addresses the characteristics and management style of leadership, is too subjective and could result in firms making judgments that would not produce the intended result. He encouraged the ISQM 1 TF to adjust the factor such that it is more neutral.</p>	<p>Point partially accepted.</p> <p>Ms. Corden acknowledged the suggestion and explained that this factor was intended to address how the firm's culture and commitment to quality are driven by leadership. She suggested that some of the explanations in the application material could be moved to the requirement to clarify its intent.</p>

<sup>4</sup> ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

<sup>5</sup> Renumbered to paragraph 25(a)(i)(c) in Agenda Item B1.2

Representatives' Comments	ISQM 1 TF/IAASB Response
<p>Mr. Yoshii suggested that compensation, promotion and other incentives should be included in the factors in paragraphs 22E<sup>6</sup> and A24A<sup>7</sup> of proposed ISQM 1, as well as in the definition of deficiencies and in paragraph 23<sup>8</sup> of proposed ISQM 1 as part of the culture of the firm.</p>	<p>Point not accepted.</p> <p>Ms. Corden explained that compensation, promotion and other incentives are addressed in the application material to paragraph 65D<sup>9</sup> of proposed ISQM 1 and in the resources component.</p>
<p>Ms. Robert indicated that applying the factors may be challenging, and firms may develop complex matrices to map all of the factors set out in proposed ISQM 1. She added that if the intent is for the factors to be conditional, then they should not be in the requirement.</p>	<p>Point noted.</p> <p>Ms. Corden explained that the factors need to be considered because they focus on the nature and circumstances of the firm and the engagements it performs. Ms. Corden added that firms are not expected to have an elaborate matrix to demonstrate how they considered the factors, although would need to include in their documentation how they reached their conclusions on the quality risks. Ms. Corden emphasized that paragraph A214<sup>10</sup> of proposed ISQM 1 was added to clarify that firms are not expected to document every factor considered and instead focuses firms on documenting the reasons for the assessment of the quality risks.</p>
<p>Ms. Zietsman suggested clarifying paragraph 22G<sup>11</sup> of proposed ISQM 1 to improve consistency with paragraph 22D<sup>12</sup> of proposed ISQM 1 and also suggested adding application material to clarify that if the firm establishes additional quality objectives, the firm may subsequently determine that they are no longer needed.</p>	<p>Point accepted.</p> <p>Ms. Corden acknowledged the suggestions and clarified that the intent is that the firm can remove the additional quality objectives.</p> <p>Paragraph 27 of Agenda Item B1.2 was revised to improve consistency with paragraph 24 of Agenda Item B1.2, and paragraph A54 of Agenda Item B1.2 was added to clarify that a firm may identify</p>

<sup>6</sup> Renumbered to paragraph 25 in Agenda Item B1.2

<sup>7</sup> Renumbered to paragraph A32 in Agenda Item B1.2

<sup>8</sup> Renumbered to paragraph 28 in Agenda Item B1.2

<sup>9</sup> Renumbered to paragraph 56 in Agenda Item B1.2

<sup>10</sup> Renumbered to paragraph A204 in Agenda Item B1.2

<sup>11</sup> Renumbered to paragraph 27 in Agenda Item B1.2

<sup>12</sup> Renumbered to paragraph 24 in Agenda Item B1.2

Representatives' Comments	ISQM 1 TF/IAASB Response
	information that indicates that additional quality objectives are no longer needed.
Mr. James encouraged the ISQM 1 TF to undertake a post implementation review of proposed ISQM 1 and enquire from firms what additional quality objectives were established, in order to identify best practices and possible additional quality objectives that may need to be included in the standard.	Point noted.
MONITORING AND REMEDIATION	
Mr. Dalkin asked Ms. Corden to clarify how the severity and pervasiveness of deficiencies is addressed in proposed ISQM 1, emphasizing the importance of this concept so that firms are not sidetracked by immaterial issues.	Ms. Corden explained that the evaluation of deficiencies would be undertaken individually and in aggregate, similar to how the evaluation of misstatements would be undertaken in an audit. Ms. Corden added that there could be deficiencies which on their own do not affect the achievement of a quality objective, however when aggregated with other deficiencies may affect the achievement of a quality objective. Ms. Corden further clarified that the overall evaluation of the system of quality management is affected by the severity and pervasiveness of deficiencies, as well as other considerations such as the root cause and remediation of the deficiency. Ms. Corden noted that it is important that deficiencies are identified because it drives continual improvement.
Ms. Zietsman supported the direction of this component, adding that the changes have been responsive to the feedback from respondents to ED-ISQM 1, the CAG and the IAASB.	Support noted.
Ms. Zietsman provided various suggestions on paragraphs 44 <sup>13</sup> and 45 <sup>14</sup> of proposed ISQM 1. With respect to paragraph 44 she suggested a more explicit reference to monitoring the monitoring activities and questioned the need for	Point accepted.  Paragraph A144 of <b>Agenda Item B1.2</b> was added to clarify the expectations with respect to monitoring the monitoring activities, with a focus on the design of the monitoring and remediation

<sup>13</sup> Renumbered to paragraph 37 in Agenda Item B1.2

<sup>14</sup> Renumbered to paragraph 38 in Agenda Item B1.2

Representatives' Comments	ISQM 1 TF/IAASB Response
<p>referring to ongoing and periodic monitoring activities, explaining that it could be difficult to measure “appropriate” in this context and that some firms may not need to undertake ongoing monitoring activities. With respect to paragraph 45, she indicated that the reference to paragraph 44 was confusing and seemed circular, and that there may be different layers in thinking about the matters in paragraph 44.</p>	<p>process. In particular, it includes an example that contrasts how a less complex, and more complex firm may approach this, in order to demonstrate scalability.</p> <p>The reference to ongoing and period monitoring activities was removed from the requirement and relocated to application material to explain that monitoring activities may comprise a combination of ongoing and periodic monitoring activities.</p> <p>Paragraph 38 of <b>Agenda Item B1.2</b> was restructured to further clarify the intent of the requirement and the various factors that would be taken into consideration in determine which engagements and engagement partners should be selected for inspection, including the factors in paragraph 37 of <b>Agenda Item B1.2</b>.</p>
<p>Ms. Zietsman commented on the definitions of findings and deficiencies. With respect to the definition of deficiencies, she supported the application material but raised concern that the definition is not clear, and that an appropriate threshold is needed to support consistent application. With respect to the definition of findings, she suggested that the description in part (ii) (“that indicates that one or more deficiencies may exist”) should also apply to part (i). Mr. Hirai also commented on the relationship between findings and deficiencies, indicating that the difference between findings and deficiencies is not clear, and encouraged the ISQM 1 TF to develop a flowchart or guidance of how to evaluate findings and deficiencies.</p>	<p>Point accepted.</p> <p>Ms. Corden indicated that the definitions would be a key point of discussion for the IAASB in the upcoming meeting.</p> <p>The definition of deficiencies in paragraph 16(a) of <b>Agenda Item B1.2</b> has been further clarified and an appropriate threshold has been included for each element within the definition (i.e., quality objective, quality risk, response and other aspect) to support determining whether or not a deficiency exists.</p> <p>The definition of findings in paragraph 16(h) of <b>Agenda Item B1.2</b> has also been revised, and the two parts have been combined to respond to the suggestion. Application material has been added to emphasize the point that information accumulated from the performance of monitoring activities, external inspections and other relevant sources may be broader than just findings, i.e., it may include positive outcomes or opportunities for the firm to improve, or further enhance, the system of quality management.</p>

Representatives' Comments	ISQM 1 TF/IAASB Response
	<p>A depiction of the relationship between findings and deficiencies and how they are considered in the monitoring and remediation process was developed and presented to the <a href="#">IAASB in Agenda Item 5 of the June 2020 IAASB meeting</a>. The diagram will be considered for implementation guidance.</p>
<p>Mr. Hirai indicated support for retaining the reference to three years in the application material for the inspection of completed engagements, however indicated that there is not a need to take into consideration scalability of this application material.</p>	<p>Point partially accepted.</p> <p>The reference to three years in the application material for inspection of completed engagements has been retained (paragraph A153 of <b>Agenda Item B1.2</b>); however, it is an example that demonstrates the <i>principle</i> that the cyclical basis is determined by the firm based on various conditions and circumstances.</p>
<p>Mr. Ruthman sought clarity on whether the IAASB had considered the objectivity of the individuals assigned operational responsibility for monitoring and remediation from the individuals assigned ultimate responsibility for the system of quality management. Ms. Landell-Mills agreed with the view, emphasizing that from an investor perspective, it is important that the firm has independent monitoring.</p>	<p>Point not accepted.</p> <p>Ms. Klonaridis explained that the requirements in paragraph 22AA<sup>15</sup> of proposed ISQM 1 apply to the individuals assigned operational responsibility for monitoring and remediation, and also drew attention to paragraph 46<sup>16</sup> of proposed ISQM 1 addressing the objectivity of the individuals performing the monitoring activities. Ms. Klonaridis added that respondent feedback to the ED had highlighted concerns regarding the prescriptiveness of the requirements addressing the assignment of roles and responsibilities to individuals in the firm and how smaller firms would comply with such requirements, and that a requirement for the individuals assigned operational responsibility for monitoring to be objective would likely be challenging for smaller firms to implement.</p> <p>Furthermore, independent monitoring is achieved through regulatory inspection and auditor oversight.</p>

<sup>15</sup> Renumbered to paragraph 21 in Agenda Item B1.2

<sup>16</sup> Renumbered to paragraph 39 in Agenda Item B1.2

Representatives' Comments	ISQM 1 TF/IAASB Response
EVALUATION OF THE SYSTEM OF QUALITY MANAGEMENT	
Mr. Hirai indicated support for how the standard addresses the evaluation of the system of quality management. He suggested that the explanation in paragraph 27 of Agenda Item 4 of the March 2020 IAASB meeting should be included in the introduction of proposed ISQM 1 to promote proactiveness in identifying deficiencies.	Point accepted.  The explanation in paragraph 27 of Agenda Item 4 of the March 2020 IAASB meeting was incorporated into paragraph A138 of <b>Agenda Item B1.2</b> to promote proactiveness in identifying deficiencies.
EXTERNAL COMMUNICATION	
Ms. Zietsman supported how proposed ISQM 1 addresses transparency reports and encouraged the IAASB to continue to monitor and engage in conversations on this topic. She explained that while transparency reports provide visibility, it is a complex and evolving topic and it is not the role of the IAASB to define what is a transparency report or what it should include, as there is a lack of global consistency and agreement in what the concept means, what should be communicated and the extent to which matters should be prescribed. She added that if the IAASB did define transparency reports or the information to be included in the reports, it could stifle innovation that is organically taking place. Ms. Zietsman further explained that proposed ISQM 1 is dealing with the establishment of a system, and while a transparency report is related to that, the preparation of a transparency report is not core to the fundamental objective of the standard. She therefore cautioned that further efforts to consider or address transparency reports could inadvertently distract and derail the ISQM 1 project overall. Mr. Dalkin agreed and emphasized that Europe is further ahead than other jurisdictions, and that in the public sector it could be challenging to develop a report that is geared towards a firm. Mr. Hansen highlighted that transparency reports should not be promotional documents and cautioned that until such time as	Support noted.  As highlighted above in this cover note, following the March 2020 IAASB CAG meeting, the IAASB agreed to include a more explicit requirement for the firm to communicate externally.

Representatives' Comments	ISQM 1 TF/IAASB Response
audit quality indicators as more well developed and accepted, it will be challenging to drive consistency in how firms communicate externally.	
<p>Ms. Landell-Mills indicated that investors welcome transparency reports, which are important to informing investors and providing a mechanism to bring investors closer to auditors. Mr. Ruthman also encouraged a more explicit requirement for transparency reports. Both Ms. Landell-Mills and Mr. Ruthman highlighted that transparency reports hold auditors accountable for having robust systems in place and could drive a more effective system of quality management. Ms. Landell-Mills further suggested that firms should have the transparency reports assured, and the need for a framework to be developed to support consistency and comparability of transparency reports. Ms. Robert also indicated support for more open communication, however highlighted the need for the standard to be clearer about what information should be communicated. Mr. Yoshii indicated support for communication externally but emphasized that it is important to rather focus on what information should be disclosed, instead of what the form of communication is called. He cautioned that should the standard require transparency reports without specifying the content, the content disclosed could be poor. He suggested that the IAASB highlight transparency reports or audit quality reports as best practice and that the IAASB continue to consider what type of information should be disclosed.</p>	<p>Point noted.</p> <p>As highlighted above in this cover note, following the March 2020 IAASB CAG meeting, the IAASB agreed to include a more explicit requirement for the firm to communicate externally.</p>
Mr. Yoshii suggested that paragraph A151 <sup>17</sup> of proposed ISQM 1 also include information about staff compensation.	<p>Point not accepted.</p> <p>The ISQM 1 TF is of the view that information about staff compensation is covered by the categories of information described in paragraph A126 of <b>Agenda Item B1.2</b>. The ISQM 1 TF is further of the view that adding this to the application material</p>

<sup>17</sup> Renumbered to paragraph A126 in Agenda Item B1.2

Representatives' Comments	ISQM 1 TF/IAASB Response
	would result in it being overly specific in the context of the principles-based approach to describing the information that may be communicated.
NETWORK REQUIREMENTS OR NETWORK SERVICES	
Mr. De Tullio enquired about circumstances when network firms adapt or supplement the network requirements or network services, and whether the network would be expected to consider whether changes should be made at the network level, i.e., that such adaptations or supplementations may be indicative of a need for the network requirements or network services to be updated.	Point accepted.  Paragraph A179 of <b>Agenda Item B1.2</b> has been added, which focuses on the firm communicating possible improvements to the network requirements or network services.
Ms. Landell-Mills indicated that not enough had been done on networks, and enquired whether it is clear to external stakeholders that there could be a variation in quality across a network. She also enquired about the communication of key audit matters and how this has improved communication with investors about quality.	Point noted.  Ms. Corden indicated the need to obtain feedback from users about the usefulness of communication of key audit matters, which would form part of the IAASB's planned auditor reporting post implementation review.  Paragraph 51 of <b>Agenda Item B1.2</b> was amended since ED-ISQM 1 to encourage a focus on appropriate implementation across the network, since it requires the firm to understand the overall scope of the monitoring activities undertaken by the network to determine that network requirements have been appropriately implemented, and to obtain information from the network about the results of these monitoring activities.
Ms. Zietsman recognized the efforts of the ISQM 1 TF in advancing this topic. She added that a network level standard would be challenging, and that it would be difficult to enforce such a standard. She further noted her support for addressing the firm's reliance on the network by emphasizing the accountability of the firm for its system of quality management, including the firm's understanding of the network requirements or network services and what the network expects of the firm. Ms. Zietsman	Support noted.



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<p>noted that indirect pressure would be placed on the network through proposed ISQM 1, particularly related to consistency across the network as networks would need to support firms' implementation of the standard and improve information sharing. She added that the PCAOB's outreach with larger networks has revealed significant effort in preparing for the standard, and that networks have realized the benefit of implementing the standard centrally.</p>	
<p>SCALABILITY, TAILORING THE SYSTEM OF QUALITY MANAGEMENT, COMPLEXITY, PRESCRIPTIVENESS AND DEVELOPING A STANDARD THAT CAN BE APPLIED IN ALL CIRCUMSTANCES</p>	
<p>Mr. Thompson acknowledged the efforts made to address scalability and that it is an improvement from ED-ISQM 1, although indicated that he was not yet able to conclude that the latest draft is truly scalable. Mr. Thompson added that proposed ISQM 1 is a more robust and effective standard than extant ISQC 1. Ms. Robert indicated that it is difficult to assess if the standard is scalable enough and urged the IAASB to consider this in their deliberations in the upcoming March 2020 meeting, taking into account the feedback from the IFAC SMP Committee from the upcoming outreach. Mr. Thompson suggested that should it be determined that a separate standard should be developed for audits of less complex entities, it may pose a question as to whether a separate quality management standard should be developed for less complex firms.</p>	<p>Point noted.</p> <p>Ms. Corden noted Mr. Thompson's support, and indicated that it would not be possible to commit to a separate standard for less complex firms at this time.</p> <p>The ISQM 1 TF Chair and Staff held a meeting with the IFAC SMP Committee and discussed scalability of the proposed standard. The IFAC SMP Committee recognized the ISQM 1 TF's efforts to improve scalability, and supported what has been done in the firm's risk assessment process. While they questioned the scalability of the monitoring and remediation component for smaller firms, they acknowledged that it is robust.</p> <p>As part of the implementation support plan, and as noted by respondents, IAASB staff will encourage IFAC to update their <i>Guide to Quality Control for Small- and Medium-Sized Practices</i> and provide input as appropriate.</p>
<p>Mr. Pavas enquired about the development of guidance for SMPs. Ms. Robert echoed the importance of the guidance.</p>	<p>Point noted.</p> <p>Mr. Botha explained that the IAASB is working to identify the nature of implementation support material that would be provided by the IAASB, and material that should be developed by others, such</p>

Representatives' Comments	ISQM 1 TF/IAASB Response
	as IFAC and National Standard Setters. He added that if there is longer-term guidance, this would be within the remit of others. He noted that the IAASB has continued to emphasize the importance of the IFAC SMP Committee guidance. He explained that as part of the IAASB's strategy and workplan, the IAASB will continue to collaborate with others.
EFFECTIVE DATE	
<p>Mr. Pavas highlighted concern regarding the implementation date, noting the extent of changes and efforts that will be needed for implementation. Mr. Orth questioned whether the firm would need to also have tested the system of quality management by the effective date, raising concern that a December 2022 effective date could conflict with firms' busiest season.</p>	<p>Point noted.</p> <p>Ms. Corden added that the intent is firms would be expected to have the system designed and implemented by the effective date, and the cycle of monitoring and remediation and evaluation would come into effect after the effective date. Ms. Corden explained that the firm determines when the monitoring and remediation and evaluation should be undertaken, which could commence at any time throughout the year following the effective date.</p> <p>The IAASB discussed the effective date in June 2020 (see <a href="#">Agenda Item 8 of June 2020</a>) and supported the effective date of December 15, 2022.</p>
<p>Mr. Orth suggested that a December effective date may not be suitable as there are multiple activities, such as client acceptance and continuance and planning for engagement quality reviews, which should be undertaken prior to the commencement of the engagements (i.e., a December effective date would be too late in preparation for engagements with a December year-end). He therefore suggested that a June 2023 effective date may be more appropriate.</p>	<p>Point not accepted.</p> <p>Ms. Klonaridis explained that the effective date of proposed ISQM 1 will need to coincide with proposed ISA 220 (Revised) and proposed ISQM 2, and that a December date is typically used for the ISAs. Ms. Klonaridis added that irrespective of which date is selected, practically firms may need to plan ahead to take into consideration the effective date of the standards and when requirements will become applicable for the engagements performed by the firm.</p> <p>In June 2020, the Quality Management Task Forces provided a presentation to the IAASB explaining the effective dates of the three quality</p>

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	management standards and how they interrelate. See <a href="#">Agenda item 8-B of the June 2020</a> meeting.
Mr. Hirai indicated support for the how the effective date has been described in proposed ISQM 1 and further suggested more explicitly stating that within one year from the effective date, the firm is required to evaluate the system of quality management. Mr. Hirai highlighted his support for the standards to be effective as soon as possible.	Point accepted.  Paragraph 13 of <b>Agenda Item B1.2</b> , which includes the effective date, has been amended to explicitly state that the evaluation of the system of quality management is required to be performed within one year following the effective date.
OTHER COMMENTS	
Ms. Landell-Mills emphasized the importance of governance and leadership. She asked to what extent good corporate governance practices have been considered, such as the appointment of independent directors.	Point noted.  Ms. Corden explained that governance and leadership is a key aspect of proposed ISQM 1 and the standard focuses on the responsibilities of leadership of the firm. She added that in order to provide prominence to the importance of leadership's role, essential requirements have been included in the upfront requirements of proposed ISQM 1.
Mr. James asked whether the ISQM 1 TF had considered ongoing reviews being undertaken in other jurisdictions, such as the United Kingdom, Australia and the Netherlands, and whether there were any matters arising from these reviews that may inform the standard.	Point noted.  Ms. Corden noted that the ISQM 1 TF has been considering ongoing discussions in other jurisdictions as the standard is being progressed.
PIOB OBSERVER'S REMARKS	
Mr. Kashiwagi welcomed the ISQM 1 TF's efforts and acknowledged the various perspectives raised by the CAG representing a variety of stakeholder groups. He added that progress has been made in the right direction and that the draft has been improved and streamlined.	Point noted.