ED-ISQM 1 - Additional Comments

This report includes other additional comments not specific to a question in the exposure draft relating to the following aspects of ED-ISQM 1:

(a) The introduction;
(b) General requirements;
(c) The firm’s risk assessment process;
(d) Engagement performance; and
(e) The appendix.

Introduction

1. Monitoring Group

Basel Committee on Banking Supervision

ED-ISQM1: the firm's system of quality management and acceptable level of risk

ED-ISQM1 paragraph A3 explains reasonable assurance is obtained when the firm's system of quality management reduces risk to an acceptably low level. It is not clear who decides what is an acceptably low level or on what basis the decision is made.

The Committee believes that the audit firm should consider its stakeholders when making this assessment. We think the ED could be strengthened by clarifying that the acceptable low level of risk should be determined by the audit firm having regard to the public interest and the interests of the various stakeholders in the firm and, in particular, of audit, securities and financial services regulators.

International Organization of Securities Commissions (IOSCO)

The relationship between the objectives of ISQM 2 and ISA 220 with the overall objective to improve audit quality needs further attention, as ISA220 only repeats ISQM1’s objective instead of explaining their relationship. The objective of ISQM 2 does not explain how the overall objective (contained in ISQM 1) is to be achieved. A clear differentiation of the various main objectives of the three standards as well as an explanation of their interrelationship could therefore add value.

The objective at engagement level could be enhanced by stating that “the objective is to ensure that the audit is of high quality, performed in the public interest and meets all legal and regulatory requirements.”

2. Regulators and Audit Oversight Authorities

Committee of European Auditing Oversight Bodies

16. We are supportive of the concept of quality objectives, and their adaptability so as to reflect, amongst other factors, a firm’s size, complexity, structure, legal form and client base. As noted in paragraph 4 of this letter, we suggest including some of the provisions regarding scalability, which are currently part of the introductory paragraphs of the exposure draft, in the requirements section of the standard so as to better explain how the quality objectives, scalability and the risk approach are to be applied in practice and how factors such as size, complexity, structure, legal form and client base will impact a firm’s quality
management system. Additionally, as noted above, we think it is important for the standard to also address the need to learn from mistakes and errors and as a consequence we suggest adding an quality objective to ‘be a learning organization’, including the necessary requirements about an open culture and others as appropriate.

9. We feel that the introductory paragraphs to ISQM 1 provide more insight and perspective on the ambitions and intent of the new standard than the actual content of ISQM 1. We therefore suggest that the requirements and application material should be amended to fully reflect the ambitions and intentions of the new standard. For example, while the importance of taking the public interest into account is mentioned in the explanatory memorandum as one of the key points, the public interest perspective does not appear to be reflected in the objective, and not sufficiently in the requirements of the standard (it only appears in par. 23c). In the same vein, we encourage the IAASB to review the material on the risk approach and include that in the requirements and application material sections of the standard itself. In particular, we are of the view that the explanation of the risk assessment process provided in paragraph 10 of the proposed standard should be moved to the requirements section.

Independent Regulatory Board for Auditors (South Africa)

A further suggestion is that the diagrams that are included in the explanatory memorandum be included in ISQM 1. We suggest that, at a minimum, the “house” diagram on page 7 of the explanatory memorandum be included in ISQM 1. Stakeholders were of the view that this diagram aids in understanding how the components interrelate. We see no reason in our jurisdiction why such a diagram would not be a welcome addition to the standards. We suggest that diagrams be included in the introductory paragraphs, in the application material or as supplements in the standard, not in the supporting guidance material only.

A key consideration in the implementation by firms of a system of quality management, is whether firms are guided alone by the letter of the standards, or aim also to achieve the spirit of the standards. Compliance with the requirements of the standards is a necessary benchmark, but in the realm of a risk based approach to quality management, it will be necessary for firm leadership and those with overall responsibility for the system of quality management to recognise that in their quest to achieve more than compliance in quality management, they will need to identify and implement best practice that instils the spirit of quality management.

Paragraph A3 of ED-ISQM 1 states that: “... Such limitations include reality that human judgment in decision making can be faulty and that breakdowns in the firm’s system of quality management may occur, for example, due to human error or behaviour or failures in the firm’s IT applications.” While we recognise that such language is already used elsewhere in the standards, we are concerned that this sentence in this context creates a loophole in the standard and should therefore not be included. It appears to pre-empt failures in the system of quality management and findings thereon.

We have encountered a lapse in focus on quality when firms are involved in mergers and restructuring. We therefore recommend that ISQM 1 should address the need that, before mergers or takeovers of firms become effective, the new firm must have a new system of quality management in place and that such a system is fully compliant with ISQM 1. This provision is necessary as the risk assessment process of firms is unlikely to automatically envisage the objective or a response that relates to the merger of systems of quality management from two or more firms.

We have observed the frequent use of the word “may”, in both the introductory material and the application material. We encourage the IAASB to reflect on the relevance of this usage throughout the standard, and to consider alternative language that would be more helpful in achieving consistent high quality.
Irish Auditing and Accounting Supervisory Authority

We are supportive of the concept of quality objectives, and their adaptability so as to reflect, amongst other factors, a firm’s size, complexity, structure, legal form and client base. As noted in paragraph 4 of this letter, we suggest including some of the provisions regarding scalability, which are currently part of the introductory paragraphs, in the requirements section of the standard so as to better explain how the quality objectives, scalability and risk approach are to be applied in practice and how factors such as size, complexity, structure, legal form and client base will impact a firm’s quality management system. Additionally, as noted above, we think it is important for the standard to address the need to learn from mistakes and errors and suggest adding a quality objective to ‘be a learning organisation’, including the necessary requirements regarding an open culture and others as appropriate.

We feel that the introductory paragraphs to ISQM 1 provide more insight and perspective on the goals and intent of the new standard than the actual content of ISQM 1. We therefore suggest that the requirements and application material should be amended to fully reflect the goals and intentions of the new standard. For example, while the importance of taking the public interest into account is included in the explanatory memorandum as one of the key points, the public interest perspective does not appear to be reflected in either the objective or the requirements of the standard. In the same vein, we encourage the IAASB to review the material on the risk approach in the introductory paragraphs and include it in the requirements and application material sections of the standard itself. In particular, we are of the view that the explanation of the risk assessment process provided in paragraph 10 of the proposed standard should be moved to the requirements section.

3. National Auditing Standard Setters

Australian Auditing and Assurance Standards Board

Whilst the introductory paragraphs assist with understanding the risk assessment process and helpfully explain a number of important concepts in the standard, the AUASB considers their inclusion is further evidence of ISQM 1s complexity. We would caution that extensive introductory paragraphs shouldn’t be required for all IAASB standards. The AUASB recommends that the introduction or ‘executive summary’ of the standard could be positioned outside of the standard in the form of a “first time application” guide.

While the introductory paragraphs assist with understanding the risk assessment process and helpfully explain a number of important concepts in the standard, their inclusion is further evidence of ISQM 1s complexity. We would caution that extensive introductory paragraphs shouldn’t be required for all IAASB standards. This introduction or ‘executive summary’ of the standard could be positioned outside of the standard, for example in the form of a “first time through document”.

Canadian Auditing and Assurance Standards Board

We believe the IAASB could remove paragraphs 11, A21, some of the examples in A69, A112, A122 and A188. In our opinion, these paragraphs do not add clarity or new information.

Japanese Institute of CPAs

Understandability of the standard: We are concerned that it is difficult to gain an overall understanding of the standard, including the flow of requirements, from just reading the standard. Therefore, we suggest rewriting
the Introduction section and Appendix 1 based on the descriptions in the Explanatory Memorandum. (Comment to Question 2)

We are concerned that it is difficult to gain an overall understanding of the standard, including the flow of requirements, from just reading the standard. Therefore, we suggest rewriting the Introduction section and Appendix 1 based on the descriptions in the Explanatory Memorandum.

We believe that the Introduction section and Appendix 1 of the exposure draft do not explain clearly the quality management approach in the standard, which impair the understandability of the standards. In contrast, we found that the Explanatory Memorandum is easy to understand, as it starts with descriptions of the firm’s risk assessment process. Without reading the Explanatory Memorandum, we believe that it is difficult to understand the structure of the objective of the standard, and the relationships of the eight components in the system of quality management. As the Explanatory Memorandum will not be included in the final standard, we believe that the Introduction section and Appendix 1 need revision.

In addition, we believe that it is difficult to distinguish the following similar wordings which are used in the Explanatory Memorandum and ED-ISQM 1:

- “The objective of the system of quality management” (singular “objective”): To provide the firm with reasonable assurance of the matters described in paragraphs 18(a) and (b) (the charts in paragraphs 16, 27, 31 and 37 of the Explanatory Memorandum, and paragraph 18 of ED-ISQM 1)
- “The objectives of the system of quality management” (plural “objectives”): The statements in paragraphs 18(a) and (b) (paragraph 17 of the Explanatory Memorandum, and paragraphs 7, 10(a) and 12 (last sentence) of ED-ISQM 1)
- “The purpose of a system of quality management” (“purpose”): To support the consistent performance of quality engagements, by providing the firm with reasonable assurance that the objectives of the system, stated in paragraphs 18(a) and (b), are achieved (the first sentence of paragraph 7 of ED-ISQM 1)

For the sake of clarity, the wordings “the objectives of the system of quality management” and “the purpose of a system of quality management” should be changed to other appropriate wordings. For example, with respect to paragraphs 7, 10(a) and 12 of ED-ISQM 1, we suggest the following changes:

“7. The purpose of a system of quality management is to support the consistent performance of quality engagements, by providing the firm with reasonable assurance that:

(a) 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

(b) Engagement reports issued by the firm or engagement partners are appropriate in the circumstances, the objectives of the system, stated in paragraph 18(a) and (b), are achieved.

The public interest is served by the consistent performance of quality engagements. Quality engagements are achieved through planning and performing engagements and reporting on them in accordance with professional standards and applicable legal and regulatory requirements. Achieving quality engagements involves exercising professional judgment and, when applicable to the type of engagement, exercising professional skepticism. (Ref: Para. A2–A4)
10. In taking a risk-based approach to quality management, the firm applies the firm's risk assessment process to the other components. The firm's risk assessment process consists of:

   (a) Establishing quality objectives. The quality objectives established by the firm consist of objectives that, when achieved by the firm, collectively provide the firm with achievement of reasonable assurance that the objectives of the system of quality management, stated in paragraph 18(a) and (b), are achieved...

12... The monitoring and remediation process provides information that is the basis for the evaluation of whether the objective of the system of quality management provides reasonable assurance that the objectives stated in paragraph 18(a) and (b) have been achieved."

Paragraph 1 (Relationship between ED-ISQM 1 and ED-ISQM 2)

We believe that it is unclear in ED-ISQM 1 that ED-ISQM 2 applies to the engagements for which the firm determines that the engagement quality review is required to be performed in accordance with ED-ISQM 1, and therefore ED-ISQM 2 is on the premise that the firm applies ISQM 1. In ISAs, the authority of ISAs is only described in ISA200 to avoid duplicated descriptions in other ISAs. ISQMs should be structured in the same way. To clarify the relationship between ED-ISQM 1 and ED-ISQM 2, and to simplify the standards by avoiding duplication of the descriptions, we suggest the following changes:

"1. This International Standard on Quality Management (ISQM) deals with a firm's responsibilities to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements. ISQM 2, which applies to all engagements for which an engagement quality review is required to be performed in accordance with proposed ISQM 1, deals with the responsibility of the firm and engagement quality reviewers relating to engagement quality reviews. This ISQM is to be read in conjunction with relevant ethical requirements."

With regard to our suggestion to delete duplication of the descriptions related to the above change, please see our comment on paragraph 16 below and our comment on ED-ISQM 2 (Question 2).

Paragraph 16 (Relationship between ED-ISQM 1 and ED-ISQM 2)

Paragraph 16 overlaps with paragraph 8 of ED-ISQM 2. Given that ED-ISQM 2 addresses the requirements for the engagement quality review with respect to the engagement for which an engagement quality review is required to be performed in accordance with ED-ISQM 1, we believe that the matters described in ED-ISQM 1 do not necessarily need to be repeated in ED-ISQM 2. As stated in our comment to paragraph 1 above, in order to clarify the relationship between ED-ISQM 1 and ED-ISQM 2 and to simplify the standards, we believe that paragraph 16 of ED-ISQM 1 should be changed as follows and paragraph 8 of ED-ISQM 2 should be deleted:

"Authority of this ISQMs

16. This ISQMs contains the objective of the firm in following this ISQMs, and requirements designed to enable the firm and the engagement quality reviewer (in the context of ISQM 2) to meet that stated objective...."

Kammer der Steuerberater und Wirtschaftsprufer

The volume of the proposed ED-ISQM 1 is already a challenge in itself for implementation. There is a lot of background material included, especially at the beginning of the standard. This background material, if in
fact it is needed at all, could be placed outside the standard. Indeed, the IAASB should be mindful that large volumes of material can overwhelm firms and practitioners and detract from the central messages of the standard. Additionally, no matter how voluminous the material, it will never cover all the firms’ ways of working. In terms of supporting material for implementation, an update of the ISQC 1 guidance published by the SMP committee could be useful while it might sound counterproductive and even ironic that smaller firms need more guidance to implement ED-ISQM 1.

**New Zealand Auditing and Assurance Standards Board**

In our targeted outreach in relation to ED ISQM 1 with New Zealand firms and practitioners, we heard feedback from SMPs that the objective and scope of the standard could be clarified by expanding on what is meant by related services. It may not be clear to those unfamiliar with the IAASB terminology which of the following are within scope: agreed upon procedures, compilation work, tax services, business advisory services, etc. We recommend that this term is defined.

For example, the introduction is lengthy and repeats the standard. While this may be useful initially, it will be less so as firms familiarise themselves with the changes. This overview of the standard could be positioned outside of the standard as a type of “At a Glance” summary.

**Royal Nederlandse Beroepsorganisatie van Accountants**

The various responsibilities between the firm, engagement partner, engagement quality reviewer, networks and service providers could be further clarified. The engagement partner is responsible for the opinion/conclusion for which he uses professional judgment. However, he is dependent on the support of the firm, the network and service providers to be able to do so. We recommend to make clear that networks and service providers can be very useful if their services are designed appropriately and operate effectively.

The firm is responsible for the system of quality management to enable the engagement partner taking responsibility for the engagement. As such the firm requires engagement quality reviews for certain engagements and this is a quality measure to achieve reasonable assurance at firm level. Although the need for a review is set at firm level, the engagement quality reviews are performed at the engagement level and as such are also an important quality measure at an individual engagement. Although the report for an audit may not be provided before the approval of the reviewer, the responsibility of the engagement partner is not reduced by the engagement quality reviewer. We recommend to make this more clear.

Furthermore, we have questions about the responsibilities the firms versus the individual engagement partners. This is very important for the firms in practice. Where do the responsibilities of the firm end and where do the responsibilities of the individual engagement partner begin? This might be different for certain jurisdiction, but when it comes to claims this can become a serious issue. The engagement partner is responsible for the opinion/conclusion for which he uses professional judgment. However, he needs the support of the firm, the network and service providers to be able to do so.

The quality management system of the firm should enable the engagement partner to take responsibility for the engagement. The firm is responsible for the system of quality management to ensure that the engagement partner is doing his work properly.

We also recommend to remove the duplicative texts in the application material. For example, paragraphs A6-A9 of ISQM 1 explain the authority of the standard, but could either be shortened or removed as this seems obvious.
4. Accounting Firms

**BDO International**

Potential for scope confusion

ED-ISQM 1 applies to ‘…firms performing audits or reviews of financial statements, or other assurance or related services engagements.’ During our internal and external discussions, it has become clear that there is some confusion about the scope of the standard regarding the extent to which it applies to:

- Larger audit firms - which may be structured via a holding entity with various operational entities and service lines and whether the proposed quality management approach would apply across firms or across all operational entities and service lines.
- Individuals who may not be ‘professional accountants’ but who may still perform roles within the range of engagements listed in ED-ISQM 1.

While we acknowledge that further clarification is provided in the ED-ISQM 1 objective section, the way paragraph 4 is drafted within the scope section has the potential to raise more questions than it answers.

Extending the list in paragraph A4 to include root cause analysis and also the determination of any remedial actions. Both areas are inherently based on the need to exercise professional judgement and by including them in this list it further highlights the importance of these concepts emphasised in other parts of ED-ISQM 1.

Including examples of firms applying a QMF during a period of change to support paragraph 6 (such as firm mergers, firm acquisitions, provision of new assurance service lines, changes in key personnel).

**Scalability concept**

By adopting a risk-based approach to engagement quality (recognising that there is an acceptable level of risk in any engagement), it may not be entirely appropriate to adopt the same approach for a system of quality management. Specifically, a better way of bringing in the concept of scalability may be to improve the lead-in sentence in paragraph 5 ED-ISQM 1 to state:

> ‘When approaching the design, implementation and operation of the system of quality management, this ISQM requires the firm to take into account…’

In addition:

- Within the Introduction section the sections on scalability (paragraphs 5 and 6), the firm’s system of quality management (paragraphs 7 to 13) and networks (paragraph 14) appear to be out of order. We would ask that the firm’s system of quality management section be moved up to paragraph 4, with scalability being positioned closer to the network section.
- Paragraph 11 which introduces the concept of ‘components’ should precede or be merged into current paragraph 8 so that it’s explanation is provided in an appropriate context.

**EY Global Limited**

**Paragraph A4**

Remove the first bullet “The appropriate organizational structure…” and the fifth bullet “The resources and information and communication that are appropriate…” as these are both covered by the fourth bullet “The appropriate nature, timing, and extent…”
Nexia Smith & Williamson

Language: in many places we consider the language to be wordy and over-complicated, for example:
Paragraph 10, in particular (c).

PriceWaterhouseCoopers

Paragraph 1 - The second sentence should refer to the “responsibilities” of the firm and engagement quality control reviewers, rather than “responsibility”.

Paragraph 7 - We suggest the first comma in this paragraph is not required. We also suggest referring to “the objective stated in paragraph 18” rather than “objectives stated in paragraphs 18(a) and (b)” for consistency with paragraphs 13, 16 and 18, which refer to “the objective of” this ISQM/the firm i.e., singular.

Paragraph 8 - We suggest the word “process” does not reflect the nature of a system of quality management and recommend remaining with the term “system”. We further suggest amending “and is responsive” to instead state “that is responsive”.

Paragraph 10(a) - We suggest the following clarification: “The firm is required to establish the quality objectives set out in this ISQM and additional quality objectives beyond those required by this ISQM, when those objectives are determined by the firm to be necessary to achieve the objective of this ISQM.”

Paragraph 12(c) - We suggest aligning more closely with paragraph 49: Designing and implementing remedial actions, Remediating the identified deficiencies responsive to the root causes”. See also paragraph 7 editorial suggestion with respect to objectives.

Paragraph 15 - We suggest the principle established in paragraph 14 that the firm remains responsible for its system of quality management is also relevant here and is consistent with paragraph 64: “This ISQM also includes requirements for circumstances when the firm intends to obtain or use resources provided by a service provider in its system of quality management. Notwithstanding the firm’s use of a service provider(s), the firm remains responsible for its system of quality management”.

Paragraph A3 - We suggest that “reality” is not necessary in this sentence. See also paragraph 7 editorial suggestion with respect objectives.

Paragraph A4 - Bullet 2 - See editorial suggestion on paragraph 10(a). Bullet 6 - see editorial suggestion on paragraph 7.

6. Member Bodies and Other Professional Organizations

Chartered Accountants Australian and New Zealand and ACCA

ED-ISQM1 does not provide any information in respect of what constitutes ‘related services’. We therefore would consider it beneficial for greater clarity on this.

CPA Australia

The requirements are not necessarily as clear as the introduction and may not be able to stand alone, which we consider they should. The introductory material provides a helpful overview of the standards and in some cases is clearer than the requirements themselves. We suggest that the IAASB check that each of the introductory statements is fully reflected in the requirements so reliance does not need to be placed on the introduction to understand the intention of the requirements. As the introduction in effect summarises or repeats the requirements, we suggest that this material could instead be repurposed. The introductions to all
of the standards could be combined into an explanatory document which provides a useful overview of how all of the standards fit together and what they require.

**Institute of Chartered Accountants in England and Wales**

The following comments are on paragraphs that are unnecessarily obvious, verbose, repetitive, circular or otherwise hard to understand (or apparently illogical) as a result of the clumsy use of language. They are simply those that have been brought to our attention and do not represent a comprehensive analysis.

Para 10, (c) in particular, (verbose)

**General requirements**

**3. National Auditing Standard Setters**

Canadian Auditing and Assurance Standards Board

We believe the IAASB could remove paragraphs 11, A21, some of the examples in A69, A112, A122 and A188. In our opinion, these paragraphs do not add clarity or new information.

**Japanese Institute of CPAs**

- **Consistency between ED-ISQM 1 (paragraph 20) and ED-ISQM 2 (paragraph 12):** We believe that it is necessary to consider consistency between paragraph 20 of ED-ISQM 1 and paragraph 12 of ED-ISQM 2 with regard to who is required to have an understanding of the standards. (Comment to paragraph 12)

- The third sentence of A12, A21, A31, A32, the last sentence of A34, A35, A36, A39, A41, A57, A94, A97, A116, A121, A122, A137, A154, the first sentence of A172, the last paragraph of A180, A187 (excluding the last paragraph), and A188

- Paragraph 20

(Consistency with paragraph 12 of ED-ISQM 2)

We believe that consistency between paragraph 20 of ED-ISQM 1 and paragraph 12 of ED-ISQM 2 needs to be reconsidered. Paragraph 12 of ED-ISQM 2 requires the firm as well as engagement quality reviewer to have an understanding of ISQM 2, while paragraph 20 of ED-ISQM 1 requires the individual(s) assigned ultimate responsibility and accountability, and the individual(s) assigned operational responsibility, for the firm's system of quality management to have an understanding of ISQM 1. Therefore, there is inconsistency between those requirements with regard to the treatment of “the firm.”

(Required understanding of the individual(s) assigned ultimate responsibility and accountability)

Paragraph 20 states that the individual(s) assigned ultimate responsibility and accountability and the individual(s) assigned operational responsibility, are required to have an understanding of ISQM 1 relevant to their responsibilities. To avoid the misunderstanding that merely a superficial understanding is sufficient, we suggest the following changes:

"20. The individual(s) assigned ultimate responsibility and accountability, and the individual(s) assigned operational responsibility, for the firm's system of quality management shall have an understanding of this ISQM relevant in order to fulfill their responsibilities, including the application and other explanatory material, to understand the objective of this ISQM and to apply its requirements properly."
New Zealand Auditing and Assurance Standards Board

Remove non “shall” statements from the requirements

Para 22. Remove the second sentence “The requirements are designed to enable the firm to achieve the objective stated in this ISQM. The proper application of the requirements in this ISQM is expected to provide a sufficient basis for the achievement of the objective of this standard.” Neither of these sentences are requirements. It is superfluous to state that the requirements enable the firm to achieve the objective.

Para 45 – Engagement inspections may include the inspection of in-process or completed engagements, this is better positioned in application material as it is not required.

Royal Nederlandse Beroepsorganisatie van Accountants

Another example is paragraph A21 of ISQM 1 where paragraph 55 is repeated.

4. Accounting Firms

Baker Tilly International

ED-ISQM1.42c requires the individual assigned ultimate responsibility for the SOQM to evaluate whether the system provides reasonable assurance that objectives will be achieved. We cannot see how the individual assigned ultimate responsibility can evaluate reasonable assurance without having a detailed understanding of the standard (see comments elsewhere regarding ED-ISQM1.20).

Please see comments elsewhere where we have expressed a concern that the individual with ultimate responsibility is required to evaluate the SOQM but is not required to have an in-depth understanding of the standard. We cannot envisage how these two requirements are compatible.

BDO International

‘Tone in the middle’ concept

One area that we did think lacked clarity in ED-ISQM 1 was the ‘tone in the middle’ concept that was envisioned when the standard was first proposed for revision. Paragraph 20 ED-ISQM 1 states:

‘The individual(s) assigned ultimate responsibility and accountability, and the individual(s) assigned operational responsibility, for the firm’s system of quality management shall have an understanding of this ISQM relevant to their responsibilities, including the application and other explanatory material, to understand the objective of this ISQM and to apply its requirements properly.’

While the paragraph speaks to the responsibility of those assigned operating responsibility for the firm’s system of quality control there may be a need for ED-ISQM 1 to be broader, so that this is not treated as the responsibility of solely one individual or one department that is somehow apart from the business management or leadership of a firm. One option could be to improve the wording in this specific section to state:

‘The individual(s) assigned ultimate responsibility and accountability, (including individuals with relevant leadership roles within a firm) and the individual(s) assigned operational responsibility, for the firm’s system of quality management...’
Nexia Smith & Williamson

Paragraph A18 gives an example of using an IT application for obtaining confirmations of independence from staff. In a smaller firm, this would probably be done via email or a hard copy questionnaire, and this could usefully be acknowledged.

6. Member Bodies and Other Professional Organizations

Institute of Chartered Accountants in England and Wales

Para 20: as only one individual can be 'ultimately' responsible, we suggest that this refers to 'the individual or board assigned...'.

Firm's Risk Assessment Process

2. Regulators and Audit Oversight Authorities

Canadian Public Accountability Board

A few of the key terms in the exposure draft – objectives, risks, responses and deficiencies – are defined, but at a high level; the lack of specificity makes it harder to practically implement and test the system of quality management for operating effectiveness.

The key attributes of the system of quality management should be properly defined to enable the firms to design a system that is effective in responding to their risks. We explore below how more clearly defined expectations for design, implementation and operation would substantially improve on the practical applicability of the standard.

Committee of European Auditing Oversight Bodies

11. We note that a significant volume of detail is provided in the application material to ISQM 1. Given that the requirements by themselves should provide clear direction for auditors, we suggest that the IAASB should carefully review whether some of the application material is of such importance to enable the understanding of the requirements that the content could provide additional clarity in the requirements section. For instance, we suggest the IAASB considers whether the concept of granularity in paragraph A49 may be included in paragraph 26 of the requirements section. Also we suggest elevating the provisions in paragraph A59, on responses to assessed quality risks, to a requirement. Given the importance of also considering positive quality instances, we feel that there should be a requirement for firms to evaluate positive quality instances as well (currently only suggested in paragraph A173).

We feel that the introductory paragraphs to ISQM 1 provide more insight and perspective on the ambitions and intent of the new standard than the actual content of ISQM 1. We therefore suggest that the requirements and application material should be amended to fully reflect the ambitions and intentions of the new standard. For example, while the importance of taking the public interest into account is mentioned in the explanatory memorandum as one of the key points, the public interest perspective does not appear to be reflected in the objective, and not sufficiently in the requirements of the standard (it only appears in par. 23c). In the same vein, we encourage the IAASB to review the material on the risk approach and include that in the requirements and application material sections of the standard itself. In particular, we are of the view that the explanation of the risk assessment process provided in paragraph 10 of the proposed standard should be moved to the requirements section.
Irish Auditing and Accounting Supervisory Authority

We note that a significant volume of detail is provided in the application material to ISQM 1. Given that the requirements by themselves should provide clear direction for auditors, we suggest that the IAASB should carefully review whether some of the application material is of such importance to enable the understanding of the requirements that it should be included in the requirements section. For instance, we suggest the IAASB considers whether the concept of granularity in paragraph A49 may be included in paragraph 26 of the requirements section. Also we suggest elevating the provisions in paragraph A59, on responses to assessed quality risks, to a requirement. Given the importance of considering positive quality instances, we feel that there should be a requirement for firms to evaluate positive quality instances (currently this is only suggested in paragraph A173).

We feel that the introductory paragraphs to ISQM 1 provide more insight and perspective on the goals and intent of the new standard than the actual content of ISQM 1. We therefore suggest that the requirements and application material should be amended to fully reflect the goals and intentions of the new standard. For example, while the importance of taking the public interest into account is included in the explanatory memorandum as one of the key points, the public interest perspective does not appear to be reflected in either the objective or the requirements of the standard. In the same vein, we encourage the IAASB to review the material on the risk approach in the introductory paragraphs and include it in the requirements and application material sections of the standard itself. In particular, we are of the view that the explanation of the risk assessment process provided in paragraph 10 of the proposed standard should be moved to the requirements section.

National Association of State Boards of Accountancy

We found the definition of “quality objectives” in Paragraph 19(p) to be circular. We recommend the definition of “quality objectives” as the objectives that, when achieved by the firm, collectively provide the firm with reasonable assurance that the objectives of the system of quality management as defined in Paragraph 19(v) have been achieved.

3. National Auditing Standard Setters

Australian Auditing and Assurance Standards Board

There are several application material paragraphs that are duplicative of requirements or establish requirements, for example A49 and A59.

Japanese Institute of CPAs

We suggest that the IAASB reconsider whether the following guidance is really necessary, as we believe they are not useful.

The third sentence of A12, A21, A31, A32, the last sentence of A34, A35, A36, A39, A41, A57, A94, A97, A116, A121, A122, A137, A154, the first sentence of A172, the last paragraph of A180, A187 (excluding the last paragraph), and A188

4. Accounting Firms

Grant Thornton International Limited

Paragraphs A49 and A59 of ED-ISQM 1 begin by identifying the paragraphs that contain the required objectives and the required responses. If, per our recommendation below, a single paragraph that
specifically requires that a firm’s system of quality management to incorporate all the quality objectives and responses in ED-ISQM 1 and to establish additional quality objectives and responses necessary that are specific to the firm’s circumstances, is incorporated into the standard, we are of the view that these paragraphs could be deleted.

KPMG IFRG Limited

However, the definition of responses currently included with the ED includes policies or procedures, but does not explicitly refer to controls. We would welcome further clarification of the meaning of the view that “responses to quality risks are analogous to controls” as included in paragraph 36 of the Explanatory Memorandum, and encourage the Board to reflect this concept in paragraphs A59-64 of the Application Guidance.

Mazars

Some aspects of the standards may also create challenges for implementation and further guidance should be given to help all firms to be in line with the principles (definition of “quality objectives” (ISQM 1), definition of a “deficiency” (ISSM 1), examples of “quality indicators” to be put in place (ISQM 1), definition of the audit team and consideration of joint audit (ISA 220)).

Nexia Smith & Williamson

The definition of “quality objectives” in paragraph 19(p) seems circular – objectives providing assurance that objectives are achieved.

PriceWaterhouseCoopers

Paragraph 26 - See editorial suggestion on paragraph 10(a).

Paragraph A21 - See paragraph 7 editorial suggestion with respect to objectives.

5. Public Sector Organizations

US Government Accountability Office

Definition of “policies” (para. 19(t)(i)): The definition of “policies” includes the following statement: “Such statements may be documented, explicitly stated in communications or implied through actions and decisions.” We believe that “implied through actions and decisions” should be removed. Engagement team members need to be able to access policies to be able to identify or confirm the proper response when they encounter a quality risk. In addition, written policies provide individuals performing monitoring procedures with objective criteria against which to evaluate a firm's performance and adherence to the policies. If this phrase is retained, we suggest that the IAASB consider emphasizing, in appropriate paragraphs of the standard, the need to maintain sufficient evidence to demonstrate that the actions or decisions are the policy of the audit organization.

6. Member Bodies and Other Professional Organizations

Belgian Institute of Registered Auditors IBR-IRE

The following A-paragraphs could for example be removed: A12 to A16, A55, A83, A85, A86, A90, A91, A94 to A97, A100, A105, A114, A115, A116. In particular, A59 is a repetition of the requirement (par. 10 c). Par. A59 could be removed and A69 should be an A-paragraph linked to par. 10 (c).
Institute of Chartered Accountants in England and Wales

The following comments are on paragraphs that are unnecessarily obvious, verbose, repetitive, circular or otherwise hard to understand (or apparently illogical) as a result of the clumsy use of language. They are simply those that have been brought to our attention and do not represent a comprehensive analysis.

The definition of ’quality objectives’ in para 19(p) (circular)

The example in para A51 (verbose)

9. Individuals and Others

Shady Fouad Ahmed Mehelba

I have noticed that paragraph A63 use the complexity of firm's structure and geographical dispersion as a factor for documentation. I believe that complexity of the firm itself or nature of engagement, rather than documentation, will have more effects on quality management. So, I suggest simplifying the process for that firms with less complex structure by restricting investigation to the most relevant root causes for identified risks, in cost effective manner, while maintaining adequate designed policies and procedures for each component of quality management. Firms with less complex structure are those that do not provide audit services to publicly listed companies or significant public interest entities and are not geographically dispersed.

Engagement Performance

1. Monitoring Group

Basel Committee on Banking Supervision

Pre-issuance technical reviews of banks’ financial statements

We note that some audit firms perform pre-issuance technical reviews of banks’ financial statements. Given banks’ central role in contributing to financial stability and providing financial resources to the economy, we believe that all bank audits should be subject to a pre-issuance technical review. Paragraphs 36 and 37 of ED-ISQM 1 could be enhanced by including an additional requirement in this respect.

International Association of Insurance Supervisors

Component auditors

Insurance groups may have several audit firms that contribute to a group audit, particularly where an insurer has international operations. In these cases, the audit firms used may or may not be part of the same audit network. There is currently no explicit text in the exposure drafts which set out the interaction of the group and component auditor in relation to quality management. As a result, it may be unclear how quality management arrangements should operate where component auditors are used. The IAASB should consider providing some additional clarity in this area.

International Organization of Securities Commissions (IOSCO)

Firms should be required to centrally monitor progress on engagements against milestones to ensure that audits are adequately planned and executed on a timely basis and address possible issues for quality audits with deadline pressures.
2. Regulators and Audit Oversight Authorities

Independent Regulatory Board for Auditors (South Africa)

We recommend that material regarding the archiving of working papers from specialist areas of the engagement, such as IT, be added. These working papers should form part of the engagement file. We have noted findings where the IT division of a firm had its own working papers, apart from the financial statement audit team's working papers. Only the financial statement audit team had archived its working papers in terms of the archiving policy, and the IT-related working papers had not been archived. All audit evidence should be included in the audit file and not just in the final report of the evidence extracted from the IT system. Alternatively, procedures should be documented in sufficient detail to enable an experienced auditor to come to the same conclusion without the IT-related working papers.

3. National Auditing Standard Setters

AICPA

We find the application material for engagement performance equally applicable to intellectual resources; this is an example of the interrelationship between components that could be provided in implementation guidance.

Canadian Auditing and Assurance Standards Board

We believe the IAASB could remove paragraphs 11, A21, some of the examples in A69, A112, A122 and A188. In our opinion, these paragraphs do not add clarity or new information.

Japanese Institute of CPAs

We suggest that the IAASB reconsider whether the following guidance is really necessary, as we believe they are not useful.

The third sentence of A12, A21, A31, A32, the last sentence of A34, A35, A36, A39, A41, A57, A94, A97, A116, A121, A122, A137, A154, the first sentence of A172, the last paragraph of A180, A187 (excluding the last paragraph), and A188

4. Accounting Firms

Baker Tilly International

Engagement Performance

ED-ISQM1.36(b) – although we acknowledge the fundamental importance of auditor judgment and the application of professional skepticism, it may be more appropriate requirements in this regard are established in the ISAs rather than in ED-ISQM1.

EY Global Limited

Paragraph 36(b)

The word ‘appropriate’ in “Engagement teams exercise appropriate professional judgment” is open to interpretation and is vague. Our view is that it is superfluous and thus we propose removing the word ‘appropriate’.

Paragraph 37(c)
We recommend adding to paragraph "Establishing policies or procedures addressing consultation on difficult or contentious matters or areas of significant judgment, including the …"

Since the firm is responsible for the system of quality management, we observe that the quality objectives in paragraphs 38(d) and 38 (g) in the ‘Resources’ component and all the quality objectives in the ‘Engagement performance’ component are not worded as actions of “The firm...” Instead, the quality objectives noted above in the ‘Resources’ component and all of the quality objectives within the ‘Engagement performance’ component are directed at personnel or engagement teams. This seems contradictory to both the objective of the standard, which is directed at the firm, as well as to most of the other quality objectives in ED-ISQM 1. Therefore, we recommend these quality objectives be rewritten to require action by the firm to clarify that the responsibility for achieving all the quality objectives lies with the firm.

**Nexia Smith & Williamson**

Sometimes, we consider the use of “may” to be inappropriate. For example:

Paragraph A109: “The integrity of engagement documentation may be compromised if it is altered, supplemented or deleted without the appropriate authorization to do so, or if it is permanently lost or damaged.” It is hard to see how it could not be compromised in most of these circumstances.

**5. Public Sector Organizations**

**Australasian Council of Auditors General**

If a firm or audit office establishes appropriate responses to meet the quality objective proposed at paragraph 36(b), considering the related application and other explanatory material at A94-97, this will assist in supporting the exercise of appropriate professional scepticism.

ACAG notes paragraph 36(b) states “professional judgement and, when applicable to the type of engagement, professional scepticism”. Is it the IAASB’s intention that there are types of engagements when exercising professional scepticism is not applicable?

**US Government Accountability Office**

Supervision and review (para. 37(a)): Paragraph 37(a) states, in part, that “such direction, supervision, and review is planned and performed on the basis that the work performed by less experienced members of the engagement team is directed, supervised, and reviewed by more experienced engagement team members.” We suggest that the IAASB consider whether experience is an appropriate measure for determining whether engagement team members adequately supervised work. Experience is only one driver of skill and proficiency in auditing. As such, paragraph 5.36 of the 2018 revision of generally accepted government auditing standards provides that “the audit organization should establish policies and procedures that require engagement team members with appropriate levels of skill and proficiency in auditing to supervise engagements and review work performed by other engagement team members.” We believe that considering the skill and proficiency of team members would more effectively achieve the objective of the requirement.
6. Member Bodies and Other Professional Organizations

Belgian Institute of Registered Auditors IBR-IRE

The following A-paragraphs could for example be removed: A12 to A16, A55, A83, A85, A86, A90, A91, A94 to A97, A100, A105, A114, A115, A116. In particular, A59 is a repetition of the requirement (par. 10 c). Par. A59 could be removed and A69 should be an A-paragraph linked to par. 10 (c).

Wirtschaftspruferkammer

The quality objective mentioned in Para 36c (“The engagement documentation is appropriately assembled and retained”) remains general and vague. Does this quality objective establish a separate requirement or does ISA 230 prevail?

8. Academics

UNSW Audit Research Network

Engagement Performance

Again, we support the requirement to establish quality objectives that address engagement performance. Particularly with regard to audit review, our own research and that of others (see Trotman, Bauer and Humphreys 2015 for a review of this literature) highlights the quality enhancing characteristics of audit review, and Herrbach (2001) report that the perceived quality of audit review is negatively associated with self reported instances of quality threatening behavior (e.g., inadequate team member supervision). We do note, however, the importance of the term ‘appropriate’, in that it recognizes the contingent quality impacting nature of the requirements. In this regard, we would recommend that greater elaboration on what factors may impact the appropriateness of a response be provided in the application and other explanatory material. For example, Andiola, Bedard and Westermann (2019) report the characteristics and potential impact of a good and poor review. Importantly, a poor review not only has the potential to negatively impact quality on the engagement for which the review is being conducted, but also negatively impact quality on future engagements (see also our comments on motivating engagement personnel under the heading of ‘resources’). Paragraph 36(a)(ii) refers to the ‘appropriate’ direction and supervision of the engagement team and review of the work performed. The explanatory material relating to this paragraph, however, does not address what is appropriate. Our own research (e.g., Kim and Harding 2017; Harding and Kim 2019) and that of others (e.g., Wilks 2002; Peecher, Piercy, Rich and Tubbs 2010) highlights that direction and supervision from superiors can sometimes threaten the objectivity of subordinate judgments. While our research (Kim and Harding 2017) highlights that auditors are often appropriately responding to the information value inherent in the direction provided by more knowledgeable engagement team members (and therefore to be encouraged), there remains the potential for auditors to inappropriately bias judgments in favor of the stated or inferred position of their superiors (Harding and Kim 2019). We recommend that the explanatory material, which is currently focused on supervision (paragraph A92) and review (paragraph A95) be expanded to also cover direction, including the importance of limiting direction to process rather than outcome.

Similarly, we recommend that paragraph 38(d) refer to the appropriate evaluations, compensation, promotion and other incentives (see also paragraph A122) so as to highlight the contingent impact of these actions. To illustrate, rewarding desired behavior may not always encourage that behavior. For example, Brael, Leiby and Shaefer 2019 find that rewarding the exercise of skepticism can lead to auditors exercising less skepticism in future tasks.
Appendix

2. Regulators and Audit Oversight Authorities

Committee of European Auditing Oversight Bodies

28. The status of the information regarding the eight components of a quality management set out in Appendix 1 is unclear i.e. whether it is intended to be guidance/application material or is it to be regarded as integral part of the standard.

Irish Auditing and Accounting Supervisory Authority

The status of the information regarding the eight components of a quality management set out in Appendix 1 is unclear i.e. whether it is intended to be guidance/application material or is it to be regarded as integral part of the standard.

3. National Auditing Standard Setters

AICPA

Appendix 1 to ED-ISQM 1 describes the components of a system of quality management. It is not clear what the purpose is of this appendix or who its intended users are. It does not explain the interrelationship among the components. This could easily form the basis for support material, which could include the graphics included in the Explanatory Memorandum. However, we do not believe that it should be included as an appendix to the standard.

Australian Auditing and Assurance Standards Board

The AUASB considers the appendix is educative in nature and while it provides useful information, could be positioned outside of the standard in the form of a “first time application” guide.

Japanese Institute of CPAs

Understandability of the standard: We are concerned that it is difficult to gain an overall understanding of the standard, including the flow of requirements, from just reading the standard. Therefore, we suggest rewriting the Introduction section and Appendix 1 based on the descriptions in the Explanatory Memorandum. (Comment to Question 2)

4. Accounting Firms

Nexia Smith & Williamson

In Appendix 1, paragraph 5 could be expanded to help SMPs. Part (a) talks about firms with a service delivery centre, and this could be contrasted with a smaller firm where everything is done by a few personnel, making it easier to direct and supervise work and thus decreasing the quality risk.

Repetition: we note some unnecessary repetition between the main standard and the application guidance, which simply increases the overall length of the material. For example, most of paragraph 4(b) is repeated in paragraph A23, and Appendix 1 is mostly a repeat of the main standard.

RSM International Limited

We do not understand the purpose of Appendix 1 and it does not add value to understanding ED-ISQM 1. If explanations are needed, they should be in the body of the standard or in the application paragraphs.
5. Public Sector Organizations

Australasian Council of Auditors General

ED-ISQM 1 is notably longer than the extant ISQC 1. There is an opportunity to incorporate the content from Appendix 1 into the application material to avoid duplication.

6. Member Bodies and Other Professional Organizations

Institute of Chartered Accountants in England and Wales

In Appendix 1, para 5 could be expanded to help SMPs. Para 5 (a) refers to firms with a service delivery centre, which could be contrasted with a smaller firm where everything is done by a few personnel, making it easier to direct and supervise, and thus decreasing the quality risk.