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Subject: IAASB Consultation on proposed International Standard on Quality Management 1  
(Previously International Standard on Quality Control 1)  

Dear Mr Botha,  

Accountancy Europe is pleased to provide you with its comments on the proposed International Standard on Quality Management 1 (ED-ISQM 1).  

We support the work that has been done by the IAASB to enhance quality management and are in favour of the risk assessment approach to drive quality. We have nevertheless a number of important points below that could help improve the ED and its implementation.  

As written, it is not clear what more needs to be done by audit firms in addition to what is currently performed under ISQC 1. These risks creating challenges for implementation for firms of all sizes, but for small and very small firms and networks particularly. Those with responsibility for methodology in their firms are unlikely to start with a blank sheet of paper and will seek to build upon their existing quality environment. It would therefore be helpful for the IAASB to map the changes made and explain which aspects of ED-ISQM 1 are a genuine step-up in quality management and which are just clarifying existing best application of ISQC 1. With proportionality and scalability in mind, the IAASB has the duty to make these standards not too onerous for small firms.  

Furthermore, although the approach as proposed is noted as risk-based, it is still very detailed and prescriptive. The list of quality objectives is very long and complex. Some quality objectives do not seem to be objectives, but rather the description of risks for not achieving a quality objective; we do not think that this will work in practice. We refer to our response to question 6 in the appendix below. We would favour an approach with strong and overarching objectives combined with fewer quality objectives per quality management area, and in some instances even one could be enough. Revising these quality objectives would make the standard easier to apply for SMPs.  

Separating the quality control aspect from the engagement quality review one is helpful, but by creating a separate standard for EQR, the IAASB should be cautious not to overemphasise the role of the EQR, as opposed to the role of the firm and the role of the engagement partner. An EQR is only
one possible response to quality risks in engagements and not in all circumstances the most effective one.

As you will see in our response to ED-220, we would welcome better clarity between the responsibilities of the different actors within the internal quality chain, being the engagement partner, the EQCR and the audit firm and network. This would impact ED-ISQM 1 as well.

Sincerely,

[Signature]

Olivier Boutellis-Taft
Chief Executive

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Accountancy Europe unites 51 professional organisations from 36 countries that represent 1 million professional accountants, auditors and advisors. They make numbers work for people. Accountancy Europe translates their daily experience to inform the public policy debate in Europe and beyond.

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APPENDIX

OVERALL QUESTIONS

Question 1 - Does ED-ISQM 1 substantively enhance firms’ management of engagement quality, and at the same time improve the scalability of the standard? In particular:

a) Do you support the new quality management approach? If not, what specific attributes of this approach do you not support and why?

b) In your view, will the proposals generate benefits for engagement quality as intended, including supporting the appropriate exercise of professional skepticism at the engagement level? If not, what further actions should the IAASB take to improve the standard?

c) Are the requirements and application material of proposed ED-ISQM 1 scalable such that they can be applied by firms of varying size, complexity and circumstances? If not, what further actions should the IAASB take to improve the scalability of the standard?

1) We support the work that has been done by the IAASB to enhance quality management and are in favour of the risk assessment approach to drive quality. We recognise the need for audit quality to be incorportated within the audit process at an earlier stage. Separating the overall quality control aspect from the engagement quality review (EQR) one is also helpful. Nevertheless, as explained in our response to ISQM 2, by creating a separate standard for EQR, the IAASB should be cautious not to overemphasise the role of the EQR, as opposed to the role of the firm and the role of the engagement partner. An EQR is only one possible response to quality risks in engagements and not in all circumstances the most effective one.

2) Many large firms are already managing quality using a similar approach to that proposed by ISQM1, in a way that is consistent with their own overall objectives and strategies. In this context, the IAASB should recognize somewhere in ED-ISQM 1 the importance of aligning quality management with individual firms’ overall strategies.

3) Despite the desire to follow a risk assessment approach, the draft appears to have the intent to cover everything in prescriptive detail. This makes the process as proposed rather prescriptive, not providing sufficient room for flexibility. In particular, the long list of quality objectives is very detailed and overcomplex. As the approach lacks simplicity, we fear it will lead to inconsistency and will generate scalability issues. As an attempt to solve this, we would favour an approach with strong and overarching objectives combined with fewer quality objectives – and even trying in some instances to have only one - per quality management area.

4) Smaller firms, in particular, are likely to need further help in the implementation phase, with wider communication and material, in order to avoid any significant issues with the application of the standards in their environment. This implementation material should focus on the proportionality and scalability elements of the standard’s application. These issues might not be isolated to smaller firms though; the IAASB should also consider mid-tier firms as they might also miss have less developed compliance functions and procedures.

5) The use of the low threshold as proposed in ISA 315 for the identification of quality risks (i.e., “more than remote likelihood”) will give rise to practical issues. Such a low threshold will result in an overly compliance-based approach on the part of firms who seek to satisfy regulators’ demands, but in so doing, may fail to really focus on the true drivers of quality. The statement in A54 “[…] not every quality risk needs to be identified and further assessed…” is key. We think that it should be clearly stated in the standard itself.
(6) It is important to note that the proposed revised standard is more than double the length of the existing one, and that is without taking into account the newly developed ISQM 2.

(7) Additionally, we suspect ISQM 1 as drafted may create a significant amount of additional documentation, especially in documenting what has not been done and why; partly as a result of the levels of prescription and detail, noted above. Documentation is important but this aspect of it looks like a compliance exercise and we are sceptical that it would help enhance quality. Overall, we think that the IAASB needs to provide more guidance on what need to be documented. The mix of requirements and guidance leads to confusion when it comes to documentation.

Question 2 - Are there any aspects of the standard that may create challenges for implementation? If so, are there particular enhancements to the standard or support materials that would assist in addressing these challenges?

(8) Firms who provide applicable services other than audit (e.g. compilations), and who are required to follow ISQM 1 as proposed, will find themselves with a significant cost burden. The risk therefore is that ISQM 1 is less likely to be adopted by firms when there is no jurisdictional requirement to do so. If the IAASB intends to develop standards suitable for all professional services, these standards need to be appropriate for firms that do not perform audits at all.

(9) It is not clear what more firms need to do in comparison with what is currently performed under ISQC 1 and we think that this will create challenges for implementation, perhaps especially for small firms and networks. Those with responsibility for methodology in their firms are unlikely to start with a blank sheet of paper but will seek to build upon their existing quality environment. Therefore, it would be helpful for the IAASB to reflect on how to communicate to firms which aspects of ED-ISQM 1 are a genuine step-up in quality management and which are just clarifying existing best application. This type of analysis would ease implementation and most importantly avoid inconsistency.

(10) 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. Whilst it might sound counterproductive and even ironic, smaller firms will need more guidance to implement ED-ISQM 1.

(11) In terms of further enhancements needed, paragraph A59 in extant ISQC 1 includes information about original paper documentation that is electronically scanned. This paragraph provides guidance for a paperless environment. Nothing has been included in ED-ISQM 1 on this aspect, but we think it could be useful for auditors.

(12) We refer to the quality objective that address acceptance and continuance of client relationships. When requiring the firms to obtain sufficient appropriate information about the integrity and ethical values, we wonder what type of information would be considered as sufficient and appropriate, and how this requirement would work in practice and consistently at international level.

1 Guide to Quality Control for Small and Medium-Sized Practices - The purpose of the Guide is to provide practical guidance to implementing a system of quality control for SMPs.
Specific Questions

Question 3 - Is the application material in ED-ISQM 1 helpful in supporting a consistent understanding of the requirements? Are there areas where additional examples or explanations would be helpful or where the application material could be reduced?

As noted above, to support a consistent understanding, firms need to fully understand what they need to do more to comply in comparison with what is required today. Given the fact that the application material is rather voluminous, we would be in favour of reducing it while still placing this useful guidance outside the standard. The IAASB should use its new category of examples document and Frequently Asked Questions. Nevertheless, it should be clear that these examples are not to be treated as authoritative or as best practice, and that there are just examples.

Specific Questions

Question 4 - Do you support the eight components and the structure of ED-ISQM 1?

We broadly support the concepts of the components and the structure of ED-ISQM 1, but we have a number of concerns that we elaborate below.

The diagram illustrates well the approach put in place and conveys much better than words the structure and the components. The IAASB could consider including it in the standard.

We think that ‘risk assessment process’ should not be considered as a component and wonder whether ‘monitoring’ and ‘governance and leadership’ should follow a different treatment as well. They are linked to processes but not components per se. In any case, a lot of the cross-referencing and complexity would be reduced if the IAASB would classify ‘risk assessment’ out of the components and treat it as an overarching process. We are also not fully convinced that a separate quality objective is necessary for ‘information and communication’. In any case, there is a lot of overlap between components that generate confusion and potential inconsistency in practice.

Nevertheless, ISQM 1 has inherited a part of the control activities’ components from ISA 315 (Revised), but in different places. We appreciate that the problem resides in the fact that with ED-ISQM 1 we are applying ‘risk assessment’, which is an auditing concept for audit firms, but both should reconcile. We should try to reduce the level of inconsistencies and explain the remaining differences, if any.

Question 5 - Do you support the objective of the standard, which includes the objective of the system of quality management? Furthermore, do you agree with how the standard explains the firm’s role relating to the public interest and is it clear how achieving the objective of the standard relates to the firm’s public interest role?

We support an objective of the standard that would be about ensuring that the firm is performing quality work. It would indeed be much more straightforward for the objective to be output orientated and aligned to the individual firm’s overall strategy, rather than process orientated.

There is no need to explain more about the firm’s role relating to the public interest; paragraph 7 is explicit enough. Standards and laws are designed to be operated within the public interest and it is in this context that firms should be delivering qualitative services.
(20) Also, the IESBA Code, as mentioned in paragraph A2, contains requirements and application material for professional accountants that enable them to meet their responsibility to act in the public interest. The current project about Role and Mindset is even emphasising this aspect of the IESBA Code.

Question 6 - Do you believe that application of a risk assessment process will drive firms to establish appropriate quality objectives, quality risks and responses, such that the objective of the standard is achieved? In particular:

(21) We think that application of a risk assessment process has the potential to drive firms to establish quality objectives, quality risks and responses, such that the firm is able to deliver quality.

(22) The language is clear, but there is a way to go before this potential is achieved. Based on the comments made above, we are not confident that the application of ISQM 1 as drafted will drive consistency around the globe.

a) Do you agree that the firm’s risk assessment process should be applied to the other components of the system of quality management?

b) Do you support the approach for establishing quality objectives? In particular:

i. Are the required quality objectives appropriate?

(23) As mentioned above, in our response to Question 1, the list of quality objectives is very detailed and we would favour an approach with much fewer quality objectives – and even trying in some instances to have only one - per quality management area, but strong and overarching objectives.

(24) Some quality objectives are not written as objectives, but rather risks for not achieving a quality objective. We refer for instance to the one included in paragraph 34 c) about the firm’s financial and operational priorities not leading to inappropriate judgement. We wonder how this can be treated as a quality objective, and how the firm can fulfil it and demonstrate it in practice.

ii. Is it clear that the firm is expected to establish additional quality objectives beyond those required by the standard in certain circumstances?

(25) It seems clear in ED-ISQM 1 that the firm is expected to establish additional quality objectives beyond those required, in certain circumstances only. It would improve scalability if the IAASB made it clear that, for many smaller firms, no additional objectives are likely to be needed. It is important to take into account the fact that these additional quality objectives will most probably be more subjective ones that will need to be properly justified as they might raise questions from regulators.

(c) Do you support the process for the identification and assessment of quality risks?

(26) The process for the identification and assessment of quality risks is very prescriptive and does not provide the necessary flexibility in its application. From the scalability perspective, it is likely to be challenging to apply. Large firms may well have plentiful resources with the required specialist skillsets, many SMPs, and potentially some mid-tier firms, on the other hand are less likely to have such resources.

(27) Paragraphs 26 to 29, dealing with the firm’s risk assessment process, are not properly structured. We understand that the proposed ISQM 1 has inherited the risk identification process of ISA 315 as recently exposed by the Board.
We mentioned in our response to the ISA 315 ED that we did not support the introduction of PCAOB terminology that we find inappropriate in an ISA environment. While the notion of ‘reasonable possibility’ is helpful in explaining the level of likelihood, a different term should be used because of its connotations with standards issued by the PCAOB. In addition, associating this notion with the wording ‘more than remote’ is confusing in an ISA environment. It implies a lower threshold than the ISA term ‘acceptably low level’ and will confuse practitioners.

(28) d) Do you support the approach that requires the firm to design and implement responses to address the assessed quality risks? In particular:
   i. Do you believe that this approach will result in a firm designing and implementing responses that are tailored to and appropriately address the assessed quality risks?

The approach has been designed based on required and extensive quality objectives. We wonder how this approach responds to objectives where there is no risk.

(29) ii. Is it clear that in all circumstances the firm is expected to design and implement responses in addition to those required by the standard?

Yes, it is clear. It seems clear in ED-ISQM 1 that the firm is expected to establish additional quality objectives beyond those required, in certain circumstances only. It would improve scalability if the IAASB made it clear that, for many smaller firms, no additional objectives are likely to be needed.

(30) Question 7 - Do the revisions to the standard appropriately address firm governance and the responsibilities of firm leadership? If not, what further enhancements are needed?

Yes, we agree. We think though that there would be merit in recognising the interdependency between the firm responsibility and the engagement partner responsibility. We refer to our letter responding to ED-ISA 220 in this context.

(31) Question 8 - With respect to matters regarding relevant ethical requirements:

a) Should ED-ISQM 1 require firms to assign responsibility for relevant ethical requirements to an individual in the firm? If so, should the firm also be required to assign responsibility for compliance with independence requirements to an individual?

b) Does the standard appropriately address the responsibilities of the firm regarding the independence of other firms or persons within the network?

Yes, we agree and think that this is consistent with the IESBA Code that includes in paragraph 900.3 that many of the provisions of Part 4B do not prescribe the specific responsibility of individuals within the firm for actions related to independence, instead referring to “firm” for ease of reference. Firms assign responsibility for a particular action to an individual or a group of individuals (such as an assurance team) in accordance with ISQC 1. In addition, an individual professional accountant remains responsible for compliance with any provisions that apply to that accountant’s activities, interests or relationships.

(32) A number of practitioners have told us that understanding the accountability of the network vs the accountability of the firm could be challenging in practice.

(33)
At a detailed level, regarding paragraph 34 (whereby “the firm shall obtain sufficient appropriate information about the nature and circumstances of the engagement and the integrity and ethical values of the client, […]”), the concept is useful, but the wording referring to the integrity of the client is so open ended that we do not believe it is appropriately used in a professional standard against which regulators will measure firms against.

Question 9 - Has ED-ISQM 1 been appropriately modernized to address the use of technology by firms in the system of quality management?

We welcome the reference to the use of technology. Technology could always be addressed in greater detail, but we are conscious that SMPs are not at the same stage as larger firms in terms of access to and use of technology. Adding on these aspects might represent information overload for SMPs. For the aspects around the alternative audit delivery models, we refer to our response to ED-220 as we think it is more appropriate to deal with them there.

For ED-ISQM 1 and its application in an SMP environment, coordination with national standard setters could be of great value as each jurisdiction might develop a tool to help smaller firms to put in place a system of quality management.

Question 10 - Do the requirements for communication with external parties promote the exchange of valuable and insightful information about the firm’s system of quality management with the firm’s stakeholders? In particular, will the proposals encourage firms to communicate, via a transparency report or otherwise, when it is appropriate to do so?

Communication with external parties and the issuance of transparency reports are aspects that are regulated by local jurisdictions. We do not think that the standard will significantly affect behaviour in this area; firms will follow what is required in their own jurisdiction, or not.

Question 11 - Do you agree with the proposals addressing the scope of engagements that should be subject to an engagement quality review? In your view, will the requirements result in the proper identification of engagements to be subject to an engagement quality review?

The IAASB has introduced the term “significant public interest”. This is critical to this Standard, but not to the other Standards in which it is found. Without further elaboration, it is likely to give rise to inconsistencies in application. Indeed, “significant” is a term that is used extensively in auditing standards. However, public interest is not and the concept is still being developed and debated.

As emphasised in our response to ED-ISQM 2, putting in place an engagement quality review is not the only response to quality risks and not in all circumstances the most effective one. With this new concept introduced with “significant public interest”, engagement quality reviews seem to be seen as the silver bullet.
Question 12 - In your view, will the proposals for monitoring and remediation improve the robustness of firms’ monitoring and remediation? In particular

a) Will the proposals improve firms’ monitoring of the system of quality management as a whole and promote more proactive and effective monitoring activities, including encouraging the development of innovative monitoring techniques?

b) Do you agree with the IAASB’s conclusion to retain the requirement for the inspection of completed engagements for each engagement partner on a cyclical basis, with enhancements to improve the flexibility of the requirement and the focus on other types of reviews?

c) Is the framework for evaluating findings and identifying deficiencies clear and do you support the definition of deficiencies?

d) Do you agree with the new requirement for the firm to investigate the root cause of deficiencies? In particular:

i. Is the nature, timing and extent of the procedures to investigate the root cause sufficiently flexible?

ii. Is the manner in which ED-ISQM 1 addresses positive findings, including addressing the root cause of positive findings, appropriate?

e) Are there any challenges that may arise in fulfilling the requirement for the individual assigned ultimate responsibility and accountability for the system of quality management to evaluate at least annually whether the system of quality management provides reasonable assurance that the objectives of the system have been achieved?

(40) The distinction between findings and deficiencies is insufficiently clear, although it is still likely that firms will see all findings as deficiencies, which is not the case.

(41) Formally evaluating annually whether the system is working is unnecessary for small firms in simple circumstances. We suggest mentioning that a three-year evaluation of the system of quality management could be sufficient for small firms.

Question 13 - Do you support the proposals addressing networks? Will the proposals appropriately address the issue of firms placing undue reliance on network requirements or network services?

(42) We support the IAASB’s proposal to address networks. From a practical point of view, we do not think it is possible to standardise it in any other way. Nevertheless, it does not mean that it will not be burdensome for all firms within a given network to comply with the requirements as set in the proposed quality management standard. The burden will be on smaller network firms to evaluate design and implementation the network’s controls that are operating in other countries. In many cases, firms could struggle in obtaining the relevant information and this situation could create a tension that would not help enhance audit quality.

Question 14 - Do you support the proposals addressing service providers?

(43) Alternative audit delivery models are not dealt with in sufficient detail. We refer to our response to Question 9.
Question 15 - With respect to national standard setters and regulators, will the change in title to “ISQM” create significant difficulties in adopting the standard at a jurisdictional level?

(44) In countries where it is explicitly mentioned into law that auditors need to follow the ISQC 1 as issued by IFAC, there will be a need to amend the reference in the law, which could be seen as an administrative burden for policy makers.

(45) We should be mindful that for some jurisdictions, the costs of translation are very high, and it would be detrimental for worldwide adoption of the IAASB suite of standards if some would not be able to afford it anymore.