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<https://www.ifac.org/publications-resources/submit-comment?exposure-draft=273188>

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Dear Willie

Comments on the IAASB's Explanatory Memorandum, *The IAASB's Exposure Drafts for Quality Management at the Firm and Engagement Level, Including Engagement Quality Reviews*

The Independent Regulatory Board for Auditors (IRBA) is both the audit regulator and national auditing standard setter in South Africa. Its statutory objectives include the protection of the public by regulating audits performed by registered auditors, and the promotion of investment and employment in South Africa.

We appreciate this opportunity to comment on the IAASB's Explanatory Memorandum, *The IAASB's Exposure Drafts for Quality Management at the Firm and Engagement Level, Including Engagement Quality Reviews*, developed by the International Auditing and Assurance Standards Board (IAASB).

We have separately provided three other letters also dated today that contain our comments on proposed ISQM 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*; proposed ISQM 2, *Engagement Quality Reviews*; and proposed revised ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*.

In the compilation of this letter we have sought the inputs of representatives from large and medium-sized firms, academics, the Auditor-General South Africa, quality management consultants, the Johannesburg Stock Exchange and the South African Institute of Chartered Accountants. Internal IRBA consultations with our Inspections and Investigations departments, brought regulatory perspectives such as an understanding of the expected impact of the proposed quality management standards on regulatory processes, and existing inspections and investigations findings related to quality management.

The comments are presented under the following sections:

- A. Overall comments;
- B. Overall questions; and
- C. General questions.

Kindly e-mail us at creintjes@irba.co.za, or phone directly on +27 87 940 8828, if further clarity is required on any of our comments.

Yours faithfully,

Signed electronically

Bernard Peter Agulhas
Chief Executive Officer

A. OVERALL COMMENTS

- a) The IRBA supports and commends the IAASB's efforts to improve audit quality through the requirements to establish a new system of quality management at audit firms (firms). We believe that such actions seek to enhance the public interest role of external audit.
- b) We understand that the successful implementation of the new and revised standards will depend on the ability of the firm leadership to transform their thinking, with a focus on leadership responsibility and accountability for quality, and the need for comprehensive change management leading to changed behaviour throughout firms.

B. OVERALL QUESTIONS

Question 1

Do you support the approach and rationale for the proposed implementation period of approximately 18 months after the approval of the three standards by the Public Interest Oversight Board? If not, what is an appropriate implementation period?

- a) Paragraph 17 of ED-ISQM 1 states that "systems of quality management in compliance with this ISQM are required to be established by TBD". Our understanding is that the effective date of the final ISQM 1 will be approximately December 2021, based on current IAASB timelines and planning. ED-ISQM 1 paragraphs 55 and 56 require the individual(s) assigned ultimate responsibility and accountability for the quality management system (QMS) to evaluate *annually* whether the system of quality management provides reasonable assurance that the objectives stated in paragraph 18(a) and (b) have been achieved.
- b) It is therefore necessary to confirm what is meant by "required to be established", as stated in paragraph 17 of ED-ISQM 1. Would the first annual evaluation have to take place at the effective date of December 2021, or at the end of the first year after the effective date, December 2022, or some period in-between? If the first annual evaluation needs to take place by December 2021, the QMS needs to be fully operational and compliant with the new ISQM 1 (as well as ISQM 2 and ISA 220) by January 2021. This allows only six months for firms to develop, test, implement and adjust the new QMS, which may not be feasible (from the expected issue date of the final standards around July 2020).
- c) Representatives of large firms have indicated that preparations have commenced to develop their new IT systems as well as policies and procedures based on the requirements in ED-ISQM 1. These preparations assume that it is unlikely that there will be major changes to the final standards compared to the Exposure Drafts. We are supportive of these proactive measures. However, these firms and other firms have indicated that six months is too short, especially for their IT systems, to make any further changes based on the final quality management standards and any differences between the Exposure Drafts and final standards, and to then test these changes. If it is interpreted that "required to be established" means "the new QMS is in place and working effectively", we recognise the need for more implementation time.
- d) From a regulatory perspective, we believe that a timely and careful approach needs to be followed. This project was commenced at the time of the *Invitation to Comment, Enhancing Audit*

Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits, in December 2015, and should now be completed, without undue delay in the public interest.

- e) A further consideration is that all three standards need to be implemented concurrently; so, any delays would affect all three proposed quality management standards.
- f) Although we support the issuing of requirements driving improved quality management by firms in the public interest as soon as possible, we believe there is a balance that needs to be achieved. It is imperative that the firms properly and adequately establish their new QMS and that the QMS are working effectively before the quality management standards become effective. Preparation and readiness should not be compromised. We therefore would support a 24-month implementation period after the approval of the three standards by the PIOB. If systems are not ready, this may lead to a further deterioration in audit quality, which will not be in the public interest.
- g) Other possible considerations related to the effective date that have been proposed and that we support are:
 - To clarify that the first annual evaluation requirement must be performed by December 2022.
 - To encourage firms to have “dry runs” of their new QMSs, in parallel with the existing systems of quality control. Internal monitoring functions and audit regulators could be encouraged to perform pilot inspections in order to provide firms with early feedback on their QMSs.
 - To encourage new firms to early adopt the new and revised quality management standards.
- h) The IAASB is also urged to consider in more detail issues related to the transitional period. There will be a transitional period during which firms will have both the old and the new quality systems in place, with audit and other engagements performed across both systems. This has implications across the spectrum of ISQM elements, firms, networks and service providers, as well all parties involved in internal and external monitoring and inspection activities.

Question 2

In order to support implementation of the standards in accordance with the IAASB’s proposed effective date, what implementation materials would be most helpful, in particular for SMPs?

- a) Non-authoritative implementation guidance delivered at the same time as the quality management standards are published will be helpful.
- b) Firms supported the FAQs and the draft examples for ED-ISQM 1. Additional FAQs and draft examples would be welcomed, especially in the context of SMPs. An appropriate illustration of the whole system of quality management would be a helpful tool.
- c) Like the current “Guide to Quality Control for Small- and Medium-Sized Practices” issued by IFAC, a guide on the new quality management standards could be developed. Such a guide could include guidance on establishing quality objectives, risks and responses, and other aspects that are relevant to SMPs. In this way, the IAASB could demonstrate how the requirements are applicable to SMPs and encourage consistent application.

C. GENERAL QUESTIONS

Question 1

Developing Nations—Recognizing that many developing nations have adopted or are in the process of adopting the International Standards, the IAASB invites respondents from these nations to comment on the proposals, in particular, on any foreseeable difficulties in applying it in a developing nation environment.

- a) South Africa is considered a developing nation. One of the features of the marketplace is the significant number of SMPs, whether audit firms or those providing other professional services to which the quality management standards would apply. Some SMPs have indicated that they presently do not have the capacity or the expertise to establish the new QMS and they may approach consultants to assist them. The risk that then arises is that the SMPs do not take full responsibility for the QMS that has been developed by an external party, or they follow a tick box approach without fully understanding how integrated the QMS is, or without having identified quality risks and responses specific to their firms and circumstances.
- b) In South Africa, local audit pronouncements reference ISQC 1. These pronouncements may also be found in the auditor accreditation and eligibility rules of certain financial regulators. It will be necessary to assess the effort and time needed to align such pronouncements with proposed ISQM 1 and the other quality management standards.

Question 2

Public Sector—The IAASB welcomes input from public sector auditors on how the proposed standards affect engagements in the public sector, particularly regarding whether there are potential concerns about the applicability of the proposals to the structure and governance arrangements of public sector auditors.

- a) The Auditor-General South Africa has advised the IRBA that it will be submitting a comment letter on the new and revised quality management standards directly to the IAASB. We recognise that there are several public sector issues that require further attention by the IAASB as it finalises the quality management standards. We reaffirm the position though that a characteristic of an international standard is for the principles to be equally applicable to the private and public sectors.

Question 3

Translations—Recognizing that many respondents may intend to translate the final ISQMs and ISA for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents may note in reviewing the proposed standards.

- a) Standards are not translated in South Africa.
