

Response Template: Proposed ISQM 1

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General Comments on Proposed ISQM 1

[Please include here comments of a general nature and matters not covered by the questions below.]

Overall Questions

- 1) Does ED-ISQM 1 substantively enhance firms' management of engagement quality, and at the same time improve the scalability of the standard?

Response:

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?

Response: Yes, we support the quality management approach. ED-ISQM 1 provides a good framework for firm management to use to establish a quality management approach. However, ED-ISQM 1 does not clearly communicate how quality management is incorporated into enterprise risk management (ERM). Our view is that ERM is the primary tool for risk management and quality management is a function of risk management, therefore the quality standard should account for the firm's ERM and strategic and operational processes. In addition, the standard does not clearly incorporate features of the legislative audit community, including value-for-money or performance auditing.

- (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?

Response: As noted above, the proposal provides a strong framework for a firm to establish processes and controls over engagement quality. Firms make both quality and business decisions. These assessments are often conflicting, such as having only designated professionals complete an audit (increase in quality) and cost (business decision). ED-ISQM 1 does not incorporate significant changes to how or if a firm incorporates quality as a primary objective. If the IAASB determines quality should have an increased priority, consequences of non-compliance with standards or applicable legislation should be more explicitly stated. For example, paragraph 51(a) should state, "*Take appropriate action, including completion of omitted procedures, to comply with relevant professional standards and applicable legal and regulatory requirements; and.*" This would require firms and their

personnel to complete all applicable professional standards and applicable legal and regulatory requirements. When a firm or personnel do not comply, they would need to go back to complete any omitted standards or requirements. Such a standard would significantly increase the accountability of the firm and personnel.

Furthermore, the definition of engagement quality review (EQR) states the EQR can be “*completed on or before the dated of the engagement report.*” EQR should be performed throughout the engagement. The standard should not permit an EQR to be performed on the date of the engagement report. The definition of EQR should clearly communicate the requirement to perform the EQR throughout the engagement in order to provide the team with sufficient time and resources to incorporate the EQR’s feedback.

- (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?

Response: The proposed ED-ISQM 1 is scalable for our Office of 150 employees.

- 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?

Response: The proposed ED-ISQM 1 provides some challenges for implementation. Challenges include, but are not limited to:

- Defining entities “that are a significant public interest.” What are the expectations of a legislative audit office? All ‘clients’ of a legislative audit office are of a public interest. Clear guidance and consideration of how to define “significant public interest” is required.
- Preparing all members of governance and leadership of his or her responsibility for “the system of quality management” (paragraph 24 (a)). All members of the “firms managing board” may not have a background in assurance or be as experienced in quality management; therefore, some individuals may require significantly more time to become knowledgeable with their responsibilities.
- Implementing possible parallel changes to engagement quality reviews (ISQM 2). We recognize the benefits of issuing both ISQM 1 and ISQM 2 in parallel, however this does increase resource needs to meet both standards simultaneously. See bullet above on “significant public interest.”

- 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?

Response: The application materials are helpful to provide an understanding of requirements; however, they should be further improved by incorporating the graphics included in the Explanatory Memorandum. We specifically feel that “The Components of a System of Quality Management” (page 7) and “Objective of the Firm” flowcharts (found on multiple pages – 11, 12, 15, 24)) provide significant value.

The question explicitly asks about ‘consistency’ and we note that ED-ISQM 1 decreases consistency from the current standards because ED-ISQM 1 is more principals based versus

requirement based. ED-ISQM 1 intentionally introduces scalability and increases the use of professional judgement, which both decrease consistency.

Specific Questions

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

Response: Yes, we support the eight components of ED-ISQM 1.

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?

Response: We support the objective of the standard and agree that paragraphs 7-13 provide sufficient detail of the firm's role in relation to public interest.

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?

Response: No, we do not agree or believe that the risk assessment process will "drive" firms to establish appropriate quality objectives. Our view is that the standard provides an appropriate framework to help a firm establish quality objectives. A firm and the firm's leadership must first be committed to quality. Without this commitment, a risk assessment process will not have a significant impact on quality.

In particular:

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

Response: A firm's risk assessment process should revolve around the firm's enterprise risk management (ERM). ERM frameworks, such as COSO, enable the firm to incorporate quality management within the ERM.

(b) Do you support the approach for establishing quality objectives?

Response:

In particular:

i. Are the required quality objectives appropriate?

Response: We support the quality objectives in ED-ISQM 1.

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

Response: It is clear that the firm shall establish quality objectives sufficient for the firm to meet the overall objectives of ED-ISQM 1.

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

Response: Yes, we support the process to identify and assess quality risks.

(d) Do you support the approach that requires the firm to design and implement responses to address the assessed quality risks?

Response:

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?

Response: ED – ISQM 1 provides a framework for which firms can use to address quality risks. As noted previously, a firm's leadership must first be committed to quality. Without this commitment, a risk assessment process will not have a significant impact on quality.

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?

Response: Yes

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

Response: Yes – we agree with the responsibilities of firm leadership and firm governance.

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?

Response: Yes, an individual within the firm should be assigned responsibility for relevant ethical requirements. We note that some firms may choose or may be required to contract out or outsource some ethics or independence processes. However, we agree that someone within the firm is still responsible for the overall ethical responsibilities, including independence.

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

Response: Yes

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

Response: Yes, ED-ISQM 1 appropriately accounts for the use of technology in the system of quality management.

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?

Response: Many firms publicly report a transparency reports. The reports provide an overview of the firm(s) system of quality management. Unfortunately, the current standard and ED-ISQC 1 do not define quality. One of the biggest challenges with audit quality is that it is not clearly observable and therefore we encourage the IAASB to define quality within the standard. We recognize the difficulty in defining quality; however, this should not prevent the standard from setting an appropriate definition. The definition would need to incorporate the following:

- Does quality include an acceptable deficiency rate? Currently regulators are reporting that the deficiency rate is too high, however it is not clear what an acceptable rate would be.
- Does quality include price or cost? Is price a component of quality?
- How is public interest incorporated into quality? Public interest of public transit or plane crashes is zero. Public interest of car accidents is much higher given that car accidents happen multiple times per day and only select accidents are reported publicly versus a single plane crash, which is reported around the world.

We encourage the IAASB to define quality and require firms to report publicly against their meeting of quality. Such a standard would show that public interest is a primary component of quality and allow the public to determine quality. For example, each firm will operate with independent deficiency rates. The rates that each firm charges would be significantly impacted by their deficiency rate. Firms with lower deficiency rates would cost more and firms with higher deficiency rates will cost less. Entities and stakeholders will then select the firm that meets their needs. This approach would improve the fact that audit or assurance quality is not clearly observable.

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?

Response: ED-ISQM 1 proposes that all engagements with "significant public interest" are subject to an engagement quality review, however ED-ISQM 1 does not clearly define how "significant public interest" is applied for legislative auditors. We propose that the IAASB clearly include in the application section A101-A107 that legislative auditors should develop and define which engagements are "significant public interest" from engagements that are of "public interest." In our view, EQR should be driven by the type of engagement (financial statement audit or ISAE 3000 engagement), and the type of entity. There may be types of entities (such as entities with significant public interest) for which no EQR is necessary for the financial statement audit, but an EQR is necessary for an ISAE 3000 type engagements. An example is a public sector entity with

straightforward accounting (only grants and salary expenses) so there is no significant risk or significant public interest in the financial statement audit. However, the entity may have an important function with respect to the safety of citizens, regulation, or economic matters, and therefore ISAE 3000 engagements merit an EQR. The legislative audit office (LAO) has the knowledge and expertise to distinguish which engagements include a “significant public interest” and ED-ISQM 1 should clearly communicate that the LAO should use this knowledge and expertise to conclude on which engagements include a “significant public interest.”

12) In your view, will the proposals for monitoring and remediation improve the robustness of firms’ monitoring and remediation?

Response:

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?

Response: As stated above, ED-ISQM 1 provides each firm a framework that promotes and places an emphasis on quality. The firm needs to adopt the framework and create a culture that encourages quality based on the leadership within the firm.

(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?

Response: We agree that completed engagements should be inspected on a cyclical basis, no less than once every three years. We encourage IAASB to increase the requirements when the inspection identifies a significant deficiency. The increased requirement should include “*Take appropriate action, including completion of omitted procedures, to comply with relevant professional standards and applicable legal and regulatory requirements; and*” a decreased cyclical basis of one year for the engagement leader or partner who was responsible for the engagement that was found to include the significant deficiency.

In addition, either ED-ISQM 1 or ED-ISQM 2 need to provide clear guidance when an inspection concludes a file has failed. If no further inspections of the partner or engagement leader are completed, the inspector is concluding the file is in isolation. What support would an inspector need to support this conclusion? Alternatively, how many additional files should be reviewed for the identified partner or engagement leader?

Furthermore, IAASB should improve ED-ISQM 1 by requiring cross sectional reviews, specifically when a new standard is issued. The review could be completed either when the file is in-progress or completed depending on what stage of the engagement the standard affects. For example, changes to IAS 315 could be reviewed prior to completion of the engagement and changes to IAS 700 would likely be reviewed once the file is complete.

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

Response: We agree with the definition of deficiency. It should be noted that the definition of deficiency allows for a range of deficiencies, similar to how assurance engagements have different levels of risk (low, moderate, high).

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

Response:

In particular:

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

Response: Yes

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

Response: Yes

(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?

Response: We have not identified any significant challenges in evaluating the system of quality management on an annual basis. We note this may be difficult in firms where they have engagements that cover periods greater than one year or with engagements that occur on a cyclical basis greater than one year (e.g. once every three years). As noted above, ED-ISQM 1 does not clearly account for value for money or performance audits. These audits frequently span more than one year and it would be difficult for the individual assigned accountability for the system of quality management to reasonably assess if the objectives of the system have been achieved.

Furthermore, it should be clarified what is meant by “reasonable assurance.” “Reasonable assurance” typically implies an audit. Is the IAASB expecting the firm to complete an annual internal audit or ISA 3000 audit of the system of quality management?

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?

Response: We agree that the firm is responsible for its system of quality management. ED-ISQM 1 sufficiently communicates this requirement.

14) Do you support the proposals addressing service providers?

Response: We have no comments at this time

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?

Response: We do not anticipate the change in title creating significant difficulties.

Editorial Comments on Proposed ISQM 1

Paragraph 51(a) states “*Take appropriate action to comply with ~~relevant~~ professional standards and applicable legal and regulatory requirements; and.*” The word “relevant” should be removed. All engagements should comply with professional standards. The challenge with including “relevant” is some standards are “relevant” at a point in time. For example, ISA 260, if a practice review identifies that the audit team failed to communicate an audit plan to those charged with governance, it will be argued that it is no longer relevant; however, the communication of the audit plan during the planning of the audit is of significant importance and “relevant” during the planning stage of the audit. Removing the word “relevant” eliminates these future debates.