

REF#737722

1 July 2019

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Submitted electronically at [www.iaasb.org](http://www.iaasb.org) and to [WillieBotha@iaasb.org](mailto:WillieBotha@iaasb.org)

Dear Sir

**COMMENT LETTER ON THE IAASB'S EXPOSURE DRAFTS FOR QUALITY MANAGEMENT AT THE FIRM AND ENGAGEMENT LEVEL, INCLUDING ENGAGEMENT QUALITY REVIEWS**

The South African Institute of Chartered Accountants (SAICA) is the home of chartered accountants in South Africa – we currently have over 44,000 members from various constituencies, including members in public practice ( $\pm 30\%$ ), members in business ( $\pm 49\%$ ), in the public sector ( $\pm 4\%$ ), education ( $\pm 2.0\%$ ) and other members ( $\pm 15\%$ ). In meeting our objectives, our long-term professional interests are always in line with the public interest and responsible leadership. SAICA is currently the only professional accountancy organisation that has been accredited by the Audit Regulator in South Africa, the Independent Regulatory Board for Auditors (IRBA).

We welcome the opportunity to comment on the IAASB'S Exposure Drafts for Quality Management at the Firm and Engagement Level, including Engagement Quality Reviews (QM-EDs). We wish to express our appreciation for the work of the IAASB's Quality Control Task Forces (IAASB Task Force) in addressing the fundamental topic of quality management.

Accompanying this cover letter, please find the comments prepared by SAICA on the QM-EDs-Quality.

Please do not hesitate to contact Hayley Barker Hoogwerf ([hayleyb@saica.co.za](mailto:hayleyb@saica.co.za)) should you wish to discuss any of our comments.

Yours sincerely

*Signed electronically*

Hayley Barker Hoogwerf  
Acting Senior Executive, Assurance and Practice

### **SAICA'S Approach to Respond**

1. With the pervasive effect that the IAASB's project on Quality Management will have on all practices utilising these standards, SAICA engaged with our members to encourage firms and practitioners to closely monitor the progress made and, in line with change management, be proactive in providing feedback to SAICA on any comments that they may have; even before the exposure drafts were officially issued for comment. To this end, SAICA established the SAICA Quality Control Reference Group (SAICA Reference Group) that met continuously throughout 2018 to study the IAASB's Issues Papers relating to Quality Management.
2. An internal Working Group studied and debated the QM-EDs and prepared initial thoughts and inputs pertaining to the questions posed.
3. SAICA participated in the IRBA Quality Control Task Group (IRBA Task Group) meeting where interested parties were invited to provide their views and comments in finalising the IRBA and SAICA comment letters. The IRBA Task Group comprised representatives from the IRBA, SAICA, academia and audit firms.
4. Included in this comment letter are the details of the discussions held by the SAICA Reference Group as well as the IRBA Task Group. The purpose of including such detail is not necessarily to provide a definitive conclusion on the matters noted but rather to point out areas of concern for further consideration by the IAASB Task Force.

### **Contents**

5. The SAICA comment letter is structured in the following sections:
  - A. General comments on Proposed ISQM 1
  - B. Overall questions

## A. General Comments on Proposed ISQM 1

### *Evidence of compliance with the QM-EDs*

6. In the design and implementation of the system of quality management (SOQM), the firm is required to apply professional judgement at various stages of the process. From a monitoring point of view, significant concerns were noted around how an individual will exercise oversight in relation to the application of professional judgement in the design and implementation of the SOQM and what the firm is required to document to demonstrate compliance with the requirements.
7. While we understand the reason for the inclusion of paragraph A211, specifically as it indicates that it is neither necessary nor practicable for the firm to document every matter considered, or judgement made about the SOQM, guidance in terms of minimum documentation requirements will be most welcome. Specific areas where this is seen as being of practical importance have been highlighted as such within the applicable section.
8. To echo the point noted in Response Template: Quality Management Covering Explanatory Memorandum, strong calls for a framework or a model relating to how SMPs could comply with the requirements were heard. Such a framework or model should include guidance that can be used in documenting the outcome of the risk assessment process. To this end, we recommend that the IAASB consider whether it is possible to develop such a framework or model to support firms in implementing the standards as intended.
9. The view is that for the larger firms, how to demonstrate compliance is less of a concern because the SOQM and documented policies or procedures are such that it is less likely for requirements of ED-ISQM 1 not to apply. From a SMP point of view, it appears to be onerous for them to assess whether each aspect of ED-ISQM 1 has at least been considered. Therefore, in further addressing concerns around scalability, it is our view that the inclusion of a framework that either prescribes or illustrates the minimum documentation requirements will significantly contribute to the scalability of ED-ISQM 1. This way, firms can focus their attention on designing, implementing and operating a reliable risk assessment process that is appropriate and the need for *ticking every box* required by the standard will be mitigated.
10. It is SAICA's recommendation that the IAASB engage the International Forum of Independent Audit Regulators (IFIAR) in understanding how they intend regulating compliance with the requirements of the QM-EDs. The IAASB can then use input obtained through this engagement to develop the requested illustrative framework or model, thereby providing clarity on the minimum that is expected to be documented on an engagement file.
11. The concept of a risk based approach is not new to the auditing profession. SAICA is of the view that the mindset of the firm in approaching the proposed new and revised requirements will significantly impact the success or failure of this project. In all our outreach activities, there has been extensive focus on how the firm demonstrates compliance in relation to specific aspects of the SOQM; and rightfully so; however if this focus shifts to applying the risk based approach in designing and implementing a reliable system that operates as intended, the objectives of both a SOQM and that of ED-ISQM 1 will be achieved and the firm will indirectly achieve compliance with the standard.

## **Definitions**

### **Engagement team**

12. Please refer to the comments noted in relation to the revised definition of engagement team as included in Response Template: Proposed ISA-220.

### **Networks**

13. With respect to the definition of Networks, a question was raised around what is meant by the term *larger* in the definition of network (paragraph 19 (k)). Although the definition has not changed and the intention is to keep this definition aligned with that contained in the International Code of Ethics for Professional Accountants, there was a question around the meaning of the word larger and the implications that this will have on the requirements in relation to a network. If the network is not considered to be large, does this then mean that this is not a network as defined and therefore does not need to comply with the considerations relating to networks? It is our suggestion that this be expanded on in the application material of ED-ISQM 1.

## B. 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?

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:

14. SAICA is fully supportive of the new quality management approach. We have not identified any significant concerns with the principles relating to the quality management approach during our outreach activities.
15. A fundamental question to be answered at the end of the process is whether the proposed new and revised requirements as contained in the QM-EDs will result in an overall improvement of audit quality. Practical examples discussed during our outreach demonstrated that there is a strong behavioural perspective to quality management and that an appropriate culture needs to be created by ensuring that there are consequences for non-compliance. It was questioned whether the issue of a revised standard can influence and change behavioural traits.
16. Generally, SMPs have greater constraints in terms of resources and are less able to absorb significant cost implications. To overcome this challenge, SMPs outsource requirements; specifically those relating to quality control, which raises concerns pertaining to their responsibility and accountability for their firms' quality control systems and whether the practitioners are taking ownership of their own quality.
17. In principle, the general consensus is that the new and revised requirements will improve audit quality. However, there are practical constraints that may hinder this. The proposed new and revised requirements will result in additional work being performed and therefore an investment of additional resources in the form of time and money; particularly in terms of the risk assessment process.
18. In relation to the additional investment in resources, there is a real concern around the availability of resources required to implement the proposed new and revised requirements. Firms will experience an increase in costs, which, in all probability is a cost the firm will not be able to pass onto the client.

### ***Changes in the Nature and Circumstances of the Firm or its Engagements***

19. We note the requirements included in paragraph 31 of ED-ISQM 1 for the firm to identify changes in the nature and circumstances of the firm or its engagements and modify the quality objectives, quality risks or responses, as appropriate in response to such changes. This however, does not provide a timeframe but merely states that the firm shall identify changes in the nature and circumstances of the firm or its engagements.
20. To this end, the one area where ED-ISQM 1 could perhaps be clearer relates to how frequently the firm is required to proactively identify changes in the nature and circumstances of the firm or its engagements that may require changes to the quality objectives, quality risks or responses.

21. Paragraph 56 of ED-ISQM 1 requires the individual ultimately responsible and accountable for the SOQM to evaluate whether the SOQM provides reasonable assurance that the objectives of ED-ISQM 1 have been achieved at least annually. In line with this requirement, it is recommended that ED-ISQM 1 require the firm to proactively assess whether there has been a change in the nature and circumstances of the firm or its engagement at least annually. In addition for the firm to perform an annual assessment, it is recommended that the standard also include criteria for changes in nature and circumstances of the firm or its engagement where the firm is required to perform an assessment of the quality objectives, quality risks or responses.

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

Response:

22. SAICA is of the view that the proposals will generate benefits for engagement quality as intended.
23. With respect to the exercise of professional scepticism, SAICA envisages that the proposed new and revised requirements will support the exercise of professional scepticism at engagement level.
24. Paragraph 7 indicates that achieving the objective of the professional standards and complying with the requirements of applicable law or regulation involves exercising professional judgement, and when applicable to the type of engagement, professional scepticism. Questions were raised on numerous occasions around what is meant by *when applicable to the type of engagement*. The exercise of professional scepticism is applicable to all types of engagements, albeit to differing degrees.
25. It is our understanding that this has been added to cater for agreed-upon procedure engagements, where the exercise of professional scepticism may not necessarily be applicable. It is therefore recommended that the standard either clearly stipulate which engagements are being referred to (agreed-upon procedures) or this statement be removed.

(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:

26. SAICA recognises the various actions undertaken by the IAASB in an attempt to address the scalability of extant ISQC 1. As indicated above, we support the new risk based approach that encourages proactive management of quality. During our outreach activities, it was found that there are conflicting views about the complexity of the proposed new and revised requirements and application material. In relation to the scalability of the standards, concerns were noted and SAICA shares these concerns.
27. In terms of the complexity of ED-ISQM 1, it seems that the larger firms find it easier to understand and have identified the availability of resources as being the issue, while the smaller firms are concerned about the complexity as well as the availability of resources.
28. In expanding on our concern relating to scalability, in the IAASB's Quality Control and Group Audits Project Proposal, it was noted that consideration will be given to how extant ISQC 1 can be revised to encompass the principles of quality management, and support the ability of the standards to be

applied to a wide range of circumstances, but also retain the robustness of the existing requirements<sup>1</sup>. To this end, with all existing requirements of extant ISQC 1 having been carried over to ED-ISQM 1 and additional requirements still added on, it does not seem that scalability has been achieved.

29. In drafting ED-ISQM 1, a top down approach has been applied, where the standard has been drafted to cater for larger firms. Firms are therefore required to understand all of the requirements, assess what is not applicable, follow a filtering process in terms of removing these requirements and document the justification for this. This is the source of the concerns relating to how to evidence compliance with the QM-EDs. Furthermore, this process is tedious, time consuming and resource intensive.
30. To truly achieve scalability, a bottom up approach should be followed, where the minimum requirements are included that can then be scaled up based on the nature and circumstances of the firm and the engagements performed to cater for the larger and more complex firms. This approach will also address the concerns noted during our outreach in relation to how evidence compliance with the QM-EDs is demonstrated in that the minimum requirements will be applicable across the board and therefore the need to document rebuttable of certain requirements will not be necessary.

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:

31. As indicated in paragraph 1, ED-ISQM 1 is applicable to firms undertaking audits or reviews of financial statements, or other assurance and related services engagements. In the absence of the scope paragraphs, in reading the rest of ED-ISQM 1, an incorrect assumption that this is only applicable to audit engagements may be made in that there is a strong undertone of audit engagements throughout, with little mention to no mention of the other types of engagements.
32. It is recommended that the IAASB assess how the standard can be adapted to incorporate guidance applicable to engagements other than the audit of financial statements. In doing so, the concern relating to scalability should be kept in mind as it is possible that the requirements relating to an audit engagement are in fact too onerous in relation to other engagements included in the scope of ED-ISQM 1, namely engagements to review of financial statements, or other assurance and related services engagements.
33. During our outreach activities, the implementation challenges noted by SMPs related mainly to additional resources required for the implementation of the SOQM.
34. With respect to firms belonging to networks, a challenge was noted in that the member firm's leadership may not be operating in isolation but rather within a hierarchical management structure that reaches beyond the member firm level. A question around how ultimate responsibility for the SOQM is assigned in this instance was raised.
35. In continuing with network firms, an implementation challenge relating to the development of a risk assessment methodology and process that can be implemented consistently and result in systems of

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<sup>1</sup> Quality Control and Group Audits Project Proposal, para. 24.

quality management across a network of firms that are consistent and appropriate was raised. Although it may be possible to design such a methodology or process, this will take time to design and then test across the network firms that vary in nature and have differing circumstances. To this end, it was acknowledged that a technology solution for documenting the quality objectives, quality risks and responses for the applicable processes, as well as monitoring the responses, is also critical to drive consistent implementation throughout the network because operating systems of quality management across a network of member firms cannot be managed manually.

36. The design and implementation of a comprehensive monitoring solution is also a significant implementation challenge for a network of firms; including how to monitor network and member firm responses, the process to perform root cause and remediation and the development of an annual assessment processes. The network will have to design a monitoring process that is applied across all member firms. In the design of the monitoring solution, the network may also want to consider how to include more innovative aspects of monitoring, such as real-time monitoring elements that could improve the quality of engagements that are in-process.

37. In relation to the length of ED-ISQM 1, it is SAICA's view that the standard is not too long and that the additional application material is welcomed in providing further implementation guidance.

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:

38. The application material in ED-ISQM 1 is helpful in supporting consistent understanding of the requirements.

39. In engaging our members on the QM-EDs, a discussion around whether the paragraphs entitled *Considerations Specific to Smaller Entities* should be re-introduced. It is our understanding that that the IAASB Task Force intends drafting appendixes for each of the eight components. In light of the move by the IAASB Task Force to draft such appendixes, the general consensus was that the re-introduction of these paragraphs is not necessary if the appendixes contain guidance on how each of these elements will be practically implemented in the different circumstances that arise as a result of different firm dynamics.

40. In terms of additional examples or explanations that may be useful, a mapping, perhaps included in the appendixes of how the responses will address the objectives will be useful. It is envisaged that this mapping will illustrate a SOQM, taking into the account the minimum prescribed requirements before exercising professional judgement in adapting the system for the unique nature of circumstances of a firm.

### Specific Questions

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

Response:

41. SAICA is in support of the eight components and the structure of ED-ISQM 1 and the structure in terms of drafting a standard that is understandable.

42. There was general consensus around the order of the eight components in ED-ISQM 1 as this makes logical sense in terms of how firms will actually think about the process. The inclusion of quality



control objectives within each of the eight components, as opposed to a separate section eliminates the need for the firm to jump around the standard in identifying the requirements.

### Acceptance and Continuance of Client Relationships and Specific Engagements

43. Concerns were raised that the requirement for firms to consider the integrity of the client is not featured prominently enough. Extant ISQC 1 includes a separate requirement for the firm to consider the integrity of the client<sup>2</sup>, while ED-ISQM 1 combines the requirements for the firm to consider the integrity of the client with the step relating to obtaining information about the nature and circumstances of the engagement. To this end, we recommend that ED-ISQM 1 includes a separate, specific requirement for the firm to consider the integrity of the client.

44. ED-ISQM 1 is not clear in terms of who is ultimately responsible for the final decision in relation to whether the firm should accept/continue an engagement or not. Is this the responsibility of the firm or the engagement partner and if it is the engagement partner, when there are different engagement partners servicing one client, who makes the ultimate call? In line with assigning responsibility and accountability more definitely, it is recommended that the standard clarify this.

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:

45. SAICA supports the objective of ED-ISQM 1.

46. In relation to objectives, ED-ISQM 1 refers to the purpose of a SOQM<sup>3</sup>, being the consistent performance of quality engagements. In line with the structure of other international standards on auditing, ED-ISQM 1 also contains an objective for the firm to achieve, in this case to design, implement and operate a SOQM that provides the firm with reasonable assurance in relation to the fulfilment of responsibilities and issuing of reports<sup>4</sup>. At face value, the purpose of the SOQM and the objective of ED-ISQM 1 seem clear, but it has been identified as area of unnecessary confusion. To this end, we recommend that the IAASB integrate the purpose of the SOQM in supporting the consistent performance of quality engagements into the objective of ED-ISQM 1.

47. In line with the recommendation to align the purpose of the SOQM to the objective of ED-ISQM 1, we further suggest that the objective of ED-ISQM 1 makes specific reference to the fact that the public interest is served by the consistent performance of quality engagements.

48. Based on the outcome of the above recommendation, the IAASB may then need to relook at how paragraph 7 of ED-ISQM 1 is structured as there may be unnecessary duplication that can then be removed.

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?

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<sup>2</sup> ISQC 1, para. 26(c)

<sup>3</sup> ED-ISQM 1, para. 7

<sup>4</sup> ED-ISQM 1, para.18

Response:

49. It is generally recognised that it will take time for firms to establish the objective, identify the risks and develop the related responses. Firms consulted with indicated that the concept behind this process is something that the majority of firms are familiar with and should therefore result in appropriate quality objectives being established, quality risks identified and appropriately responded to, such that the objective of the standard is achieved.
50. A specific area of concern noted relates to how the firm demonstrates compliance with the risk assessment process as contained in ED-ISQM 1; particularly as it relates to the initial identification and filtering of risks, even before these are considered to be actual identified quality risks that need to be assessed.
51. The following views in relation to the documentation requirements were noted:
- One view in this regard stemmed from the requirements contained in paragraph A54 of ED-ISQM 1, which states:

*Under this ISQM, not every quality risk needs to be identified and further assessed. The firm identifies which quality risks need to be further assessed based on a preliminary consideration of the possibility of the quality risks occurring and the effect of the achievement of the quality objectives. Only those quality risks that meet both of the criteria in paragraph 28(a) and (b) need to be identified and further assessed.*

In line with the spirit of a risk assessment process, only risks that have the potential to impact the achievement of audit quality should be considered.

The conclusion reached here in relation to documentation is that the firm can think of many quality risks (i.e. the whole population) but is only required to document quality risks that have a more than remote possibility of occurring and effect may that may cause a quality objective not to be met. All other quality risks are not within the scope of the EM-ISQM 1 and therefore no documentation is required around these. A concern in relation to the monitoring of this was however noted.

- In contrast to the view expressed above, the risk assessment process as contained in ED-ISQM 1 was compared to the risk identification and assessment process followed by the auditor during the performance of an audit where a risk matrix is used. Here, all identified risks are documented and then assessed in terms of being significant or not. If a similar approach is not followed in the performance and documentation of the quality management risk assessment process, the firm may experience difficulty in demonstrating that certain risks were identified but not documented because they were not considered to be quality risks within the scope of the ED-ISQM 1.

Furthermore, in performing the risk assessment process, the firm is applying professional judgement and unless this process is clearly documented, the firm may again find it difficult to demonstrate compliance with ED-ISQM 1.

In assimilating this to an area where there is current ambiguity, reference is made to paragraph 26 of ISA 240 and the requirement relating to revenue recognition. The confusion in practice relates to whether the presumed significant risk is per individual assertion that is identified or is this for all assertions and the auditor is then required to document why certain assertions are not considered to be significant risks. It is envisaged that firms may experience similar confusion based on the requirements contained in ED-ISQM 1 in relation to the risk identification process.

52. It is our view that as ED-ISQM 1 is currently written, the acceptable approach in relation to documentation; particularly as it relates to risk identification and assessment is not clear and is an area that requires further clarification.
53. In taking this a step further, the monitoring of the risk assessment process, particularly as it relates to the assessment of the identified quality risk in determining whether a response is required will be challenging and a difficult assessment to make (your assessment of my assessment). This may give rise to boiler plate risks emerging.

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:

54. SAICA agrees that the firm's risk assessment process should be applied to the other components of the SOQM.

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

Response:

55. SAICA agrees with the requirement to consider whether additional quality objectives should be established based on the nature and circumstances of the firm<sup>5</sup>. This requirement enhances scalability and makes the standard more principles based. We believe that the required objectives as currently stated are sufficiently broad to enable firms to adapt these to the specific nature and circumstances of the firm.
56. There is, however a concern that the process for establishing quality objectives is not sufficiently clear. We strongly suggest that the IAASB relook at how this process can be clarified. Developing a framework for this process or establishing criteria to be applied by the firm may be solutions to addressing this. It will be particularly useful for the application material to expand on the documentation requirements in relation to the criteria considered.

In particular:

- i. Are the required quality objectives appropriate?

Response:

57. In our outreach activities, this question was raised numerous times and there was no indication of the quality objectives not being appropriate.

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

Response:

58. Paragraph 26 of ED-ISQM 1 states that the firm shall establish additional objectives beyond those required by ED-ISQM 1. It is therefore clear that the firm is expected to establish additional quality objectives beyond those required by the standard. However, the particular circumstances that would necessitate the firm to established additional quality objectives is not clear. Criteria for determining

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<sup>5</sup> ED-ISQM 1, para.26

when firms should establish additional quality objectives and examples of possible additional quality objectives would be useful in assisting firms in practically and consistently apply these requirements.

59. In relation to establishing these additional quality objectives, it is SAICA's view that the standard could provide more practical guidance around how the firm actually goes about establishing these additional quality objectives. A framework or set of criteria for how this consideration is document will also be most useful.

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

Response:

60. SAICA supports the process for the identification and assessment of quality risks. Certain practical challenges have, however been noted in this regard.
61. Firstly, ED-ISQM 1 is silent as to when and how often firms are required to assess quality risks. Paragraph A53 states that the identification and assessment process may involve a combination of ongoing and periodic procedures. It is our recommendation that a list of criteria be developed for firms to consider in determining when additional quality risks may have arisen.
62. The diagram illustrating the process for the identification and assessment of quality risks included on page 13 of the Explanatory Memorandum to ED-ISQM 1 makes reference to *quality risks (whole population)*. The concept of the *whole population* is further referred to in paragraph A175. Practically, there is uncertainty around how firms ensure that the *whole population* has been considered in the identification and assessment of quality risks.
63. ED-ISQM 1 contains no prescribed minimum quality risks and this was an area of significant debate during our outreach activities. There were conflicting views as to whether the standard should prescribe minimum quality risks or not.
64. It is SAICA's understanding that a decision to not include quality risks was taken because this merely entailed writing the response in the form of a quality risk and therefore did not add any value. In testing this, we support the IAASB's decision not to include prescribed quality risks.
65. ED-ISQM 1 does, however also not include prescribed responses to all of the components; namely *Acceptance and Continuance of Client Relationships and Specific Engagements*, as well as *Resources*. While we support the decision not to include the prescribed quality risks, we would recommend that each component at least include minimum prescribed responses that firms need to implement in addressing the identified quality risks.
66. This is also an area where minimum documentation requirements is seen as being welcomed; specifically with relation to what the firm is required to document for quality risks that may form part of the whole population but the nature of these quality risks is such that the firm does not believe that any further consideration with respect to the likelihood or impact is required.
67. In taking this a step further, we suggest that the IAASB consider providing implementation guidance on how to document the process for the identification and assessment of quality risks.
68. Paragraph A55 of ED-ISQM 1 indicates that there is a reasonable possibility of a risk occurring when the likelihood of its occurrence is more than remote. It is our understanding that the term *more than remote* has been included to address the matter of practically, where the standard is saying that the firm is not expected to note and respond to each and every risk that is identified. The term *more than remote* did however give rise to the concerns. Although we acknowledge that the firm is required to

exercise professional judgement in the identification and assessment of quality risks, it is recommended the IAASB consider either describing more clearly what is meant by the term *more than remote* or additional guidance on this be included in either the application and explanatory material or in the appendix to the standard.

69. Questions were raised around whether the assessment of a quality risk being less than remote applies when the firm is *identifying* the quality risks or whether this is applied in *assessing* the identified quality risks. Based on the current reading of the ED-ISQM 1, it appears that the assessment of a risk being less than remote is applied when identifying the quality risk. This creates uncertainty around what is required by the firm in *assessing* the quality risk if the threshold relating to the likelihood of the risk occurring has already been applied.
70. In referring to the assessment of a quality risk, it is assumed that the assessment relates to determining the nature of the risk and the required response and is no longer about the threshold. *I apply the threshold to identify the quality risks that require a response and then I assess these quality risks in determining the appropriate response.*
71. To address the confusion that seems to be prevalent among firms, it is recommended that the two requirements relating to identifying a quality risk and then assessing the quality risk be separated into two separate requirements, in line with the way ISA 315 (Revised) is proposing this be addressed.
72. Paragraph 28(b) makes reference to a quality risk having a significant effect on the achievement of the quality objectives. It is our view that further guidance on what is meant by *significant effect* is needed to clarify what the IAASB intends with this requirement.
73. In concluding our comments in relation to the risk identification and assessment process, it is our view that this is an area that firms, particularly SMPs are feeling uneasy about, in terms of how to practically apply these requirements. To this end, we would like to emphasise the importance of implementation guidance in this area; firstly to demonstrate how the IAASB envisages these requirements being practically applied and implemented and secondly to demonstrate how this step can be scaled to apply in the SMP environment.

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

Response:

74. SAICA supports the approach that requires the firm to design and implement responses to address the assessed quality risks. We believe that this approach supports the firm in the consistent performance of high quality audit engagements and ultimately achieving the objective of ED-ISQM 1
75. During our outreach activities, the question around whether the prescribed minimum responses are applicable to all firms in practice was raised numerous times. Participants were however not forthcoming in identifying specific responses that they felt should be removed.
76. In relation to the documentation of responses, paragraph A63 of ED-ISQM 1 indicates that the need for formally documented policies or procedures may be greater for firms that have many personnel or that are geographically dispersed, in order to achieve consistency across the firm. This paragraph implies that the documentation of responses does become less formal in the smaller and less complex firms, which is welcomed in line with the objective of addressing the concerns relating to scalability. However, the concern again was noted around how the firm will demonstrate compliance where formal documentation is not required in all instances. This may give rise to practical issues during the performance of both internal and external inspections.

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:

77. If implemented correctly by firms, SAICA believes that this approach will result in firms designing and implementing responses that are tailored to and appropriately address the assessed quality risks.

- 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:

78. There is a specific paragraph contained in ED-ISQM 1 that indicates that a firm is required to design and implement responses to address the assessed quality risks, including the responses required by ED-ISQM 1. Although SAICA believes that this requirement is clear, concerns have been noted that it is not clear that additional responses are required. To this end, we suggest that this requirement be clarified by using similar wording used in relation to the quality objectives; as follows:

*The firm shall design and implement responses to address the assessed quality risks. The responses to quality risks shall include those required by this ISQM, as well as any additional responses beyond those required by this ISQM, when those responses are necessary to achieve the objective of this ISQM. The design of the responses shall be based on, and responsive to, the reasons for the assessment given to the quality risks.*

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:

79. The important role that governance and leadership play in establishing an effective SOQM that results in the objective of ED-ISQM 1 being met cannot be emphasised enough. SAICA welcomes the enhancements made in ED-ISQM 1, particularly as they relate to the expected behavior of firm leadership in setting the tone at the top, the appropriate qualifications of leadership, and holding leadership accountable through performance evaluations.

80. A pertinent concern raised in relation to the implementation of ED-ISQM 1 relates to the lack of resources. To this end, we welcome that ED-ISQM 1 now addresses firm leadership's ability to influence decisions about the firm's resources.

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:

81. SAICA is in favour of the inclusion of a requirement for the firm to assign responsibility and accountability for the relevant ethical requirements to an individual within the firm. As indicated earlier in this comment letter, there is a strong behavioral aspect to achieving audit quality and compliance with ethical requirements is seen as fundamental to the consistent performance of high quality

engagements. It is our view that assigning ultimate responsibility and accountability for compliance with the relevant ethical requirements will enhance the prominence of these requirements and result in firms formally incorporating ethical requirements in the SOQM.

82. In light of our view that ED-ISQM 1 should include a requirement for the firm to assign ultimate responsibility and accountability for compliance with the relevant ethical requirements to an individual, it is our view that whether the firm should also be required to assign responsibility and accountability for compliance with independence requirements to an individual would be dependent on the nature and circumstances of the firm. In larger firms, this may be desirable in terms of the work load required in monitoring compliance and it is likely that these firms have the necessary resources for this. In considering the practicalities around this at SMPs, this may not be desirable in that the size of the firm may not lend itself to separating the responsibility for compliance with independence out of the requirement to comply with the relevant ethical requirements.
83. In line with how ED-ISQM 1 allows the individual who is ultimately responsible and accountable for the SOQM<sup>6</sup> to assign operational responsibilities for the SOQM<sup>7</sup>, we suggest that the person assigned ultimate responsibility and accountability for compliance with ethical requirements be granted the same ability to assign operational responsibility in this regard.
84. In incorporating this in ED-ISQM 1, we suggest that paragraph 24(a)(iii)(b) retain the requirement for the assignment of operational responsibility for the monitoring and remediation process. A third bullet can then be added to address assigning operational responsibility and accountability for the relevant ethical requirements.

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

Response:

85. SAICA is satisfied that ED-ISQM 1 appropriately addresses the responsibilities of the firm regarding the independence of other firms or persons within the network.

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

Response:

86. In recognising and responding to the fact that firms are increasingly using technology to facilitate the operation of their SOQM, SAICA welcomes the reference to the use of technological resources<sup>8</sup>.
87. With reference to paragraph 38(e) and to clarify the technological resources that are within the scope of ED-ISQM 1, we recommend that the standard clarify that the technological resources evaluated and documented as part of the SOQM are limited to those that are *specifically designed* to enable the SOQM and the performance of engagements.
88. However, the use of technology in the firm's SOQM poses a risk to quality in itself and it is our view that ED-ISQM 1 does not clearly caution firms in this regard. We therefore recommend that the

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<sup>6</sup> ED-ISQM 1, para. 24(a)

<sup>7</sup> ED-ISQM 1, para. 24(a)(ii)(a)

<sup>8</sup> ED-ISQM 1, para. 38(g)

IAASB consider expanding on paragraph 38(g) by stating that firms should be alert to additional risks to quality that arise in using technological resources to facilitate the operation of the SOQM.

89. In line with the increasing use of technology by firms in the SOQM, firms are required to determine whether the software that they are using is an appropriate resource. Software used may include off the shelf packages that are widely used and generally accepted as being appropriate for use, or the firm may implement custom made software. Depending on the origin of the software, the work effort required to conclude that it is an appropriate resource may differ greatly. It is our view that the standard is not clear in terms of the extent of work that the firm is required to perform in concluding that the software is appropriate.

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:

90. SAICA supports the requirements relating to information and communication and we believe that this will promote the exchange of valuable and insightful information about the firm's SOQM.

91. In relation to transparency reporting, SMPs are generally faced with a constraint on resources and are more likely to focus resources on revenue generating areas as opposed to internal administrative matters. It is therefore likely that SMPs will only produce such reports if forced to do so, through a requirement of a professional standard or other regulatory requirement.

92. During our outreach activities, it was concluded that if ED-ISQM 1 were to prescribe the issue of transparency reports, this will most likely apply to firms with a client base consisting of entities listed in paragraph 37 (e). Although this makes logical sense, the administration required in preparing a transparency report may outweigh the benefit gained from playing in the space of this specific types of entities and from a South African point of view, this may be counterproductive in addressing market concentration.

93. Our preference is therefore for ED-ISQM 1 not to prescribe the issue of transparency reports but rather encourage firms to use them as a means for external communication, as done in paragraph 41 (c)(iv) and continue to allow local law, regulation or professional standards to dictate when the firm is required to publish a transparency report, as per paragraph A142.

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:

94. SAICA agrees with the proposals addressing the scope of engagements that should be subject to an engagement quality review (EQR) and believe that these requirements will result in the proper identification of engagements subject to an EQR.

95. In relation to the requirement contained in paragraph 37(e)(ii), where reference is made to *entities that are of significant public interest* concerns were noted in that it is not clear which entities fall into this category and since there is no definition or set criteria to be applied in making this determination, it is left open for interpretation.



96. Since there is no definition for an *entity of significant public interest*, we suggest that the IAASB consider aligning the terminology to that used in the International Code of Ethics for Professional Accountants and rather refer to *public interest entities*. As allowed in paragraph A101 of ED-ISQM 1, local law or regulation can then define the which specific public interest entities are scoped into this requirement.
97. In mitigating the risk of differing interpretation, SAICA supports the guidance contained in paragraph A101 that allows local law or regulation to include different criteria or characteristics that firms may use in determining whether an entity is of significant public interest.
98. The risk of different interpretations is further mitigated by the guidance contained in paragraph A102 of ED-ISQM 1. We do suggest that the guidance contained in this paragraph be extended to include:
- Number of equity or debt holders, and
  - Number of employees.
99. In concluding, we are aware of the practical challenges that arise in relation to trying to define a public interest entity, where the meaning of this is vastly different across the international jurisdictions. We therefore support the approach that the IAASB has taken by including the requirement in broad terms and leaving the specific application thereof up to the local regulatory bodies.

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?

Response:

100. Since the SOQM, including the related monitoring and remediation is intended to be a continuous, iterative process that is proactive in responding to change, SAICA believe that the proposals will improve the robustness of the firms' monitoring and remediation.

- (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:

101. SAICA supports the retention of the requirement for the inspection of completed engagements for each engagement partner on a cyclical basis. We also note the improved flexibility of the requirement as included in paragraph A169 where it allows the firms to establish different cyclical periods for inspecting engagement partners according to the categories of engagements performed.
102. Paragraph 45 of ED-ISQM 1 indicates that engagement inspections may include the inspection of in-process engagements. Based in practical experience, members indicated that in-process reviews is an effective tool in managing audit quality in that it allows for real time monitoring and remediation of identified deficiencies.

103. There was however a concern noted in that ED-ISQM 1 is not clear as to when a firm is required to perform an inspection of engagements. Calls were heard for more concrete requirements around when this is applicable or not because there are instances where this is neither practical nor possible. A specific concern was noted for SMPs in the outlying areas and how they achieve the 3 year cycle, as suggested in paragraph A169 with the limited resources.
104. In continuing with the concerns noted in relation to SMPs, a question around what the objective is of engagement inspections and whether this is quality management at firm level or engagement level was raised. Since this is included in ED-ISQM 1, it is assumed to be a firm level response. To this end, the appropriateness of engagement inspections as a firm level monitoring tool for SMPs was questioned. In a larger firm, this monitoring tool may be effective in identifying common findings, which indicate a failure in the SOQM that can be remediated but the appropriateness of this for an SMP when they do not necessarily have this *learning aspect* was questioned.
105. Another view noted was not in support of the requirement included in paragraph 45(b) because including this very specific required response to perform inspections cyclically could lead to firms implementing an inspection process based solely on a cyclical basis, e.g., three-years and this may not be appropriate based on the assessed quality risks for the firm. The view here was that the requirement should be more principles based, in allowing the firm to tailor the response based on the identified quality risks. It was further recommended that the application guidance included in paragraph A169 be rewritten to emphasise the fact that the inspection of completed engagements should be implemented in response to the identified quality risk, rather than just being response that is blindly implemented on a cyclical basis.

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

Response:

106. Paragraph 47 of ED-ISQM 1 requires the firm to establish policies or procedures addressing the evaluation of findings to determine whether deficiencies exist. The application material then echoes the requirement for the firm to determine whether negative findings indicate that there are deficiencies in the SOQM.
107. Although paragraph A175 includes factors for a firm to consider in determining whether a finding is a deficiency, there is no clear framework for evaluating findings and identifying deficiencies.
108. This confusion is further exacerbated by the concerns noted in relation to definition of deficiency. The current definition of deficiency includes three elements of the risk assessment process; namely quality objectives, quality risks and responses to quality risks but deficiencies in each of these elements are ranked in terms of same level of seriousness. To illustrate, a missing quality objective is serious because this may result in the SOQM not achieving the overall objective; yet missing a *single* response where they may even be mitigating responses is classified on the same level as a missing objective. We do not agree with this.
109. During our outreach activities, calls were heard for a stronger framework that indicates how a firm evaluates negative findings and concludes on whether there is a deficiency in the SOQM.
110. Furthermore, guidance on whether a deficiency in one component impacts other components of the SOQM is also required. How the firm determines whether a deficiency is pervasive is also an area where calls for additional guidance were heard.

111. The interaction between an engagement level deficiency and a firm level deficiency; specifically how an engagement level deficiency impacts the firm level SOQM requires clarity.
112. The diagram included in paragraph 68 of the Explanatory Memorandum to ED-ISQM 1 provides useful insight into the intended process of evaluating findings and identifying deficiencies and we therefore recommend that this be included in the final standard.
113. Lastly, calls were heard for the inclusion of a definition of *findings* in the definitions section of the standard. The definition can be developed based on the application guidance included in paragraph A172 of ED-ISQM 1.

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

Response:

114. SAICA is in agreement with the new requirement for the firm to investigate the root cause of deficiencies. The performance of root cause analysis is not a new concept from a South African point of view. In terms of local external monitoring activities, this was introduced by the IRBA as part of a formal remedial action process, whereby firms or practitioners that received unsatisfactory inspections are requested to submit a root cause analysis and an action plan, with a written undertaking that all deficiencies that were reported to them will be addressed<sup>9</sup>. In the 2018 IRBA Public Inspections Report, it was reported that the introduction of the remedial action process have shown notable improvements by the firms in identifying the *true* root causes of findings. The ability for a firm to identify the *true* root cause of a deficiency, thereby allowing the firms to respond appropriately in our view will greatly contribute to achieving the objective of ED-ISQM 1.

In particular:

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

Response:

115. At face value, SAICA cannot see how the nature, timing and extent of the procedures to investigate the root cause are flexible. ED-ISQM 1 merely states that the firm shall establish policies and procedures addressing the investigation of the root causes of the identified deficiencies, including the nature, timing and extent of the procedures to be performed to perform such investigation<sup>10</sup>.
116. In our view, the flexibility of the nature, timing and extent of the procedure to investigate the root cause analysis will be determined by the nature and circumstances of the firm, as well as the nature and severity of the deficiency identified. Based on this view, we are satisfied that the nature, timing and extent of the procedures to investigate the root cause are sufficiently flexible.

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

Response:

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<sup>9</sup> IRBA Public Inspections Report, 2015

<sup>10</sup> ED-ISQM 1, para. 48(a)

117. In relation to positive findings, we are in support of the manner in which positive findings are addressed. The term *finding* has a negative connotation to it. We therefore suggest that the term *positive practices*, as referred to in paragraph 12 of ED-ISQM 1 be used throughout the standard and not *positive finding*, as has currently been done.

(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:

118. Paragraph 56 of ED-ISQM 1 requires the firm to undertake an evaluation of the SOQM at least annually, or more frequently, as may be required. As part of this requirement, it is not clear as to whether firms are required to reassess the established quality objectives and related quality risks on an annual, or more frequent basis, as necessary as part of this process.

119. In continuing with the requirement for the firm to reassess the established quality objectives and related quality risks, with respect to the requirement for the firm to apply a risk-based approach in the designing, implementing and operating a SOQM that take into account the nature and circumstances of the firm and the engagements performed<sup>11</sup>, the standard is not clear in terms of when a firm is required to reassess the established quality objectives.

120. ED-ISQM 1 needs to clarify when a firm is required to reassess the established quality objectives and related quality risks. Either paragraph 56 of ED-ISQM 1 needs to be clear in stating that the evaluation of the SOQM includes such a reassessment or a separate, specific requirement be included.

121. At a minimum, the firm should be required to perform an annual evaluation of the appropriateness and completeness of the firm's quality objectives. In addition, the firm should be required to reassess the established quality objectives when there is a change in the nature and circumstances of the firm or the engagements that it performed.

122. As explained above, in addition to the concerns noted on the definition of a *deficiency*, the process for a finding to become a deficiency is not clear. It is suggested that once the concerns relating to the definition of a deficiency have been addressed, the process for a finding to become a deficiency be aligned to the definition.

123. A question was raised in relating to deficiencies identified at engagement level and whether this is an indication of the firm's SOQM failing. Practically, it is commonly understood that the firm should evaluate whether a deficiency at engagement level is representative of a deficiency at firm level but this is not clear from the standards. To this end, we suggest that the IAASB clarify this in ED-220.

124. In relation to the requirement for the firm to respond to identified deficiencies, ED-ISQM 1 requires the firm to design and implement remedial action<sup>12</sup> but the timeframe of this is not clear. We therefore recommend that the IAASB consider expanding this section to include a prescribed timeframe for the implementation of such remedial action and the evaluation of the effectiveness of the related remedial action.

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<sup>11</sup> ED-ISMQ 1, para. 5

<sup>12</sup> ED-ISQM 1, para. 49

125. Paragraph 75 of the Explanatory Memorandum to ED-ISQM 1 makes reference to the firm having to perform the evaluation *at a point in time*. This concept is however not included anywhere else in ED-ISQM 1. It is recommended that the IAASB clarify the expected timing of the annual evaluation.

126. “The IAASB envisages that the evaluation would involve a determination of whether the system provides reasonable assurance that the objectives are achieved at the point in time the evaluation is undertaken.” This concept of the evaluation is as of a point in time is not included anywhere in the draft standard and should be considered as a frequently asked question in order to provide firms with a better understanding of what the IAASB intended with regards to the annual evaluation.

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:

127. SAICA is in support of the proposals addressing networks.

128. The standard is clear in stating that the firm remains responsible for its SOQM, including professional judgements made in the design, implementation and operation of the SOQM<sup>13</sup>. This requirement should result in the concern relating to firms placing undue reliance on network requirements or network services being addressed. Although in the minority, we did experience a sense that certain firms will still sit back and wait for global network firms to distribute the updated network policies or procedures that incorporate the new and revised requirements relating to quality management.

129. One area that needs to be clarified relates to firm having to *understand* certain requirements. It is not clear what is meant by this and how the firm demonstrates compliance with this requirement.

130. A question in terms of where the requirements are for the network firm to ensure that quality is consistently applied across the network was raised. The initial thought was that perhaps the requirements are imposed the wrong way around, in putting the responsibility on the firm (at the lower level) and not on the top level. In reading ED-ISQM 1 with the understanding of the concern that is being addressed, we are satisfied that it is clear that requirements relate to the individual firm and appropriately so. There, however still seems to be an element missing, relating to quality management at network level. Perhaps the ED-ISQM 1 is not the appropriate place to address this but it is our view that this is still a concern that the IAASB should consider further.

14) Do you support the proposals addressing service providers?

Response:

131. The proposals addressing service providers are most welcomed and supported by SAICA. These requirements are well thought out and practical. Engagement with practicing service providers found that many of the requirements included in ED-ISQM 1 are currently found in practice despite there being no formal requirement for them.

132. In considering whether the new requirements will create a barrier to entry into the market, it is believed that although not formally required until including these in ED-ISQM 1, it is current common

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<sup>13</sup> ED-ISQM 1, para. 58.

practice and the new requirements are therefore not likely to have a negative impact on the pool of available service providers.

133. In line with the concern in relation to limited resources available to firms to assist in the implementation of the proposed new and revised requirements, one possible solution is for firms to engage with service providers. To this end, SAICA welcomes the formalisation of the requirement in relation to using service providers.

134. In relation to technological resources, a concern in relation to the information to be obtained from the service provider was noted, specifically that included in paragraph A210 and the guidance that documentation relating to the service providers technological and intellectual resources may be requested. The view was that it is unlikely that service providers would comply with this request as it could be interpreted as a request for trade secrets. It was suggested that the IAASB re-evaluate the information that the firm will realistically be able to obtain in this regard.

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:

135. Since SAICA is not a national standard setter or regulator, we are not in a position to respond to this question.