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**Subject :** IAASB's Exposure Draft – Proposed International Standard on Quality Management 1 (Previously International Standard on Quality Control 1) – Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements

Dear Sir,

The Compagnie Nationale des Commissaires aux Comptes (CNCC) and the Conseil Supérieur de l'Ordre des Experts-Comptables (CSOEC) are pleased to provide you with their comments on the proposed International Standard on Quality Management 1 (ED-ISQM1).


We support the work done by the IAASB to enhance quality management and are in favor of the risk assessment approach to drive quality.

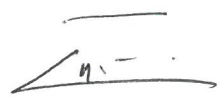
However, we are concerned about the length of the proposed standard, the requirements relating to the transparency report, the networks and the services providers.

Responses to the specific questions raised in the Consultation Paper are set out below.

If you have any further questions about our views on these matters, please do not hesitate to contact us.

Yours faithfully,

  
Jean Bouquot  
President of CNCC

  
Charles-René Tandé  
President of CSOEC

Envoyer obligatoirement toute correspondance aux deux adresses ci-dessous :

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## **Questions**

### **Overall Questions**

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

- a) Do you support the new quality management approach? If not, what specific attributes of this approach do you not support and why?*
- b) In your view, will the proposals generate benefits for engagement quality as intended, including supporting the appropriate exercise of professional skepticism at the engagement level? If not, what further actions should the IAASB take to improve the standard?*
- c) Are the requirements and application material of proposed ED-ISQM 1 scalable such that they can be applied by firms of varying size, complexity and circumstances? If not, what further actions should the IAASB take to improve the scalability of the standard?*

We support the work done by the IAASB to enhance quality management and are in favor of the risk assessment approach to drive quality.

However, we are concerned about the length of the proposed standard. We consider that the standard is too long compared to ISQM2. This forced the IAASB to develop:

- Specific FAQ regarding proposed ISQM1 and;
- Examples to explain how the nature and circumstances of the firm and the engagements it performs affect the implementation of proposed ISQM1.

We would have preferred the following option: an implementation guide and a shorter standard.

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

As mentioned hereafter, we are concerned about the following matters (introduction of PCAOB terminology in the ISAs, scalability of the proposed standard, the need of universal KPIs for the evaluation of the firm's system of quality management) and the requirements relating to:

- Transparency report
- Networks and
- Service providers.

Please refer specifically to our comments to questions 6, 9, 10, 12, 13 and 14.

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

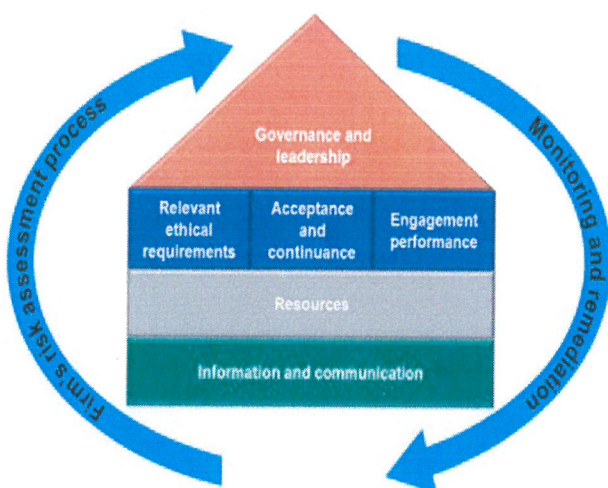
Even if we consider that the application material in ED-ISQM1 is helpful in supporting a consistent understanding of the requirements, we have specific comments. Please refer to comments on questions 4 and 14.

## Specific Questions

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

We broadly support the eight components and the structure of ED-ISQM1. However, we consider that the scheme of paragraph 11 (Page 7) of the ED-ISQM1 should be included in the application material of or in an appendix to the standard for further clarification.

The scheme is shown here below.



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

We support the objective of the standard which includes the objective of the system of quality management.

Moreover, we agree with how the standard explains the firm's role relating to the public interest and we consider that it is clear how achieving the objective of the standard relates to the firm's public interest role. We consider that there is no need to explain more about the firm's role relating to the public interest. Paragraph 7 is explicit enough.



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

We believe that application of a risk assessment process has the potential to drive firms to establish appropriate quality objectives, quality risks and responses, such that the objective of the standard is achieved.

*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?*

We agree with this statement. We consider that the paragraphs 10 (c) and A59 are clear.

"However, the responses required by this ISQM alone will not be sufficient to address all of the firm's assessed quality risks, as explained in paragraph 10 (c). Accordingly, the firm is required to design and implement responses in addition to those required by this ISQM." (cf § A59 of the proposed standard)

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

- i. *Are the required quality objectives appropriate?*

We support the approach for establishing quality objectives. In particular, we consider that the required quality objectives are appropriate.

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

It appears clear in the ED-ISQM1 that the firm is expected to establish additional quality objectives beyond those required by the standard in certain circumstances. We refer to paragraphs 26 and A50.

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

We have a concern with the introduction of PCAOB terminology that we find inappropriate in an ISA environment, especially the terms "reasonable possibility" in paragraph 28. Even if the notion of "reasonable possibility" could be helpful to explain the level of likelihood, we consider that a different term should be used because of its connotations with standards issued by PCAOB. Moreover, associating this notion with the wording "more than remote" in paragraph A55 is confusion in an ISA environment. It implies a lower threshold than the ISA term "acceptably low level" and will confuse practitioners. Moreover, there will also be a translation issue.

We therefore recommend the IAASB to remove the notion of "reasonable possibility" from the proposed standard.

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

- i. *Do you believe that this approach will result in a firm designing and implementing responses that are tailored to and appropriately address the assessed quality risks?*

We consider that this approach will result in a firm designing and implementing responses that are tailored to 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?*

We consider that it is not clear enough that in all circumstances the firm is expected to design and implement responses in addition to those required by the proposed standard. As a matter of fact:

- Paragraph 30<sup>1</sup> is not clear enough and does not include such requirement;
- There is an embedded requirement in paragraph A59<sup>2</sup> and indications are in Paragraph 10 c) but these paragraphs are non-authoritative. In particular, paragraph 10 is part of the introduction and does not specify “in all circumstances”.

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

We agree that the revisions to the standard appropriately address firm governance and the responsibilities of firm leadership. We refer to paragraphs 23 to 25.

**Question 8 - With respect to matters regarding relevant ethical requirements:**

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

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

We agree that ED-ISQM1 deals with matters regarding relevant ethical requirements.

We have no comment regarding paragraph 33 (a) that states “In designing and implementing responses to address the quality risks identified and assessed by the firm relating to the relevant ethical requirements quality objectives, the firm shall include the following responses:

(a) Identifying the relevant ethical requirements and determining the applicability of the relevant ethical requirements to the firm, its personnel and others, including, as applicable, the network, network firms, personnel in the network or network firms, or service providers. (...)”

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

We welcome the reference to the use of technology. However, we have the following concern. We consider that the requirements relating to the network and the service providers are too substantial to implement. The requirements do not seem to be sufficiently scalable. It seems cumbersome for firms in networks or using service providers to require to get a deep understanding of what is documented at the network or service provider level.

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

Communication with external parties and the issuance of transparency reports are aspects that are regulated by local jurisdictions.

In France, for example, all audit firms auditing PIEs are required to publish a transparency report. However, it is not usual for other firms to publish transparency report (e.g. firms auditing non PIEs or performing non-audit services). Based on paragraphs A148 and A149, we understand that there is no obligation for all practitioners to issue a transparency report.

<sup>1</sup> Paragraph 30 states “The firm shall design and implement responses to address the assessed quality risks, including the responses required by this ISQM. The design of the responses shall be based on, and responsive to, the reasons for the assessments given to the quality risks.

<sup>2</sup> Paragraph A59: “(...) However, the responses required by this ISQM alone will not be sufficient to address all of the firm’s assessed quality risks, as explained in paragraph 10(c). Accordingly the firm is required to design and implement responses in addition to those required by this ISQM.



With respect to paragraph A150 that gives examples of information that can be communicated to external parties about the firm's system of quality management, some indicators are usual in a transparency report, but some of them are not. This is the case, for example, for the results of inspections that are public in certain jurisdictions only. We consider that paragraph A150 is too far-reaching compared to article 13 of the regulation (EU) n°537/2014 of the European parliament and of the Council<sup>3</sup> that defines the content of the transparency report. Article 13 is principles based and is set out below. Proportionality may also be an issue.

Article 13 - " (...) 2. The annual transparency report shall include at least the following:

- (a) a description of the legal structure and ownership of the audit firm;
- (b) where the statutory auditor or the audit firm is a member of a network:
  - (i) a description of the network and the legal and structural arrangements in the network;
  - (ii) the name of each statutory auditor operating as a sole practitioner or audit firm that is a member of the network;
  - (iii) the countries in which each statutory auditor operating as a sole practitioner or audit firm that is a member of the network is qualified as a statutory auditor or has his, her or its registered office, central administration or principal place of business;
  - (iv) the total turnover achieved by the statutory auditors operating as sole practitioners and audit firms that are members of the network, resulting from the statutory audit of annual and consolidated financial statements;
- (c) a description of the governance structure of the audit firm;
- (d) a description of the internal quality control system of the statutory auditor or of the audit firm and a statement by the administrative or management body on the effectiveness of its functioning;
- (e) an indication of when the last quality assurance review referred to in Article 26 was carried out;
- (f) a list of public-interest entities for which the statutory auditor or the audit firm carried out statutory audits during the preceding financial year;
- (g) a statement concerning the statutory auditor's or the audit firm's independence practices which also confirms that an internal review of independence compliance has been conducted;
- (h) a statement on the policy followed by the statutory auditor or the audit firm concerning the continuing education of statutory auditors referred to in Article 13 of Directive 2006/43/EC; 27.5.2014 L 158/94 Official Journal of the European Union EN
- (i) information concerning the basis for the partners' remuneration in audit firms;
- (j) a description of the statutory auditor's or the audit firm's policy concerning the rotation of key audit partners and staff in accordance with Article 17(7);
- (k) where not disclosed in its financial statements within the meaning of Article 4(2) of Directive 2013/34/EU, information about the total turnover of the statutory auditor or the audit firm, divided into the following categories:
  - (i) revenues from the statutory audit of annual and consolidated financial statements of public-interest entities and entities belonging to a group of undertakings whose parent undertaking is a public-interest entity;
  - (ii) revenues from the statutory audit of annual and consolidated financial statements of other entities;
  - (iii) revenues from permitted non-audit services to entities that are audited by the statutory auditor or the audit firm; and
  - (iv) revenues from non-audit services to other entities. (...)"

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

Please refer to our comment letter on the ED-ISQM2.

<sup>3</sup> Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC

**Question 12 - In your view, will the proposals for monitoring and remediation improve the robustness of firms' monitoring and remediation? In particular:**

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

We find the proposed system very detailed and consider that standardization has limitation.

- 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?*

We 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 requirements and the focus on the other types of reviews. However, we consider that this requirement may take some time to implement.

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

We support the definition of deficiencies. However, we consider that the distinction between findings and deficiencies is insufficiently clear, although it is still likely that firms will see all findings as deficiencies, which is not the case. We consider that there may be different interpretations by the firms of the severity of deficiency.

We are concerned that it is an encouragement to publish transparency reports and that these reports include an evaluation of the firm's system of quality management. We consider that homogeneity is essential for comparability purposes. This aim can be reached only with universal KPIs. Audit quality indicators are being developed by international or European regulators that should be universal.

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

- i. *Is the nature, timing and extent of the procedures to investigate the root cause sufficiently flexible?*
- ii. *Is the manner in which ED-ISQM 1 addresses positive findings, including addressing the root cause of positive findings, appropriate?*

We have a concern with the on-going monitoring activities since we consider that it is not practicable for small practitioners.

We also believe that the work effort to be performed by each firm is high and that a core process (with core KPIs) should be developed centrally (for example by regulators) and published.

- 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?*

We consider that the IAASB should clarify that the annual evaluation of the system of quality management is not an exhaustive evaluation of the system of quality management, but rather an annual evaluation established on the basis of a multi-annual evaluation plan focused on key controls and remediation plan. We strongly recommend the IAASB to clarify this point in the proposed standard and the corresponding work effort.



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

We support in principles the IAASB's proposal to address networks. We understand the aim of the new requirements that is to improve the robustness of the firm's responsibilities for the network requirements or network services, so that the firm understands the network requirements or network services and the effect they have on the firm's system of quality management. However, we consider that the proposed requirements are too difficult and impractical to implement. We also believe that such requirements will generate duplication in work.

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

We support the proposals addressing service providers. However, we consider that it would be relevant to move paragraph 22 of the draft frequently asked questions regarding ISQM1 into the application and other explanatory material of the proposed standard. This paragraph deals with service provider and address especially the following question: Are all IT applications that are obtained from service providers subject to the requirements of paragraphs 64-65 of ED-ISQM1?

Specific attention must be paid on the reference to paragraph 65-65 in paragraph 22 of the FAQ. This has to be amended for paragraph 64-65.

Finally, we have a concern of proportionality for smaller firms that use a lot of service providers. The risk is that such requirements are totally counterproductive.

**Question 15 - With respect to national standard setters and regulators, will the change in title to "ISQM" create significant difficulties in adopting the standard at a jurisdictional level?**

We have no specific comment concerning the change in title to "ISQM".