



National Association of State Boards of Accountancy

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June 28, 2019

International Auditing and Assurance Standards Board (IAASB)  
529 Fifth Avenue  
New York, NY 10017

Via website: [www.iaasb.org](http://www.iaasb.org)

**Re: Proposed International Standard on Quality Management 1**

The National Association of State Boards of Accountancy (NASBA) appreciates the opportunity to offer comments on the Proposed International Standard on Quality Management 1 – *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements* (ED-ISQM 2). NASBA’s mission is to enhance the effectiveness of the licensing authorities for public accounting firms and certified public accountants in the United States and its territories. Our comments on the IAASB’s Exposure Draft are made in consideration of the Boards’ of Accountancy charge as regulators to promote the public interest.

In furtherance of that objective, NASBA offers the following comments on the questions as presented in the Exposure Draft.

**Overall Questions**

**Request for Comment 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?*

- (a) NASBA supports IAASB's initiatives to improve audit quality and we are supportive of the new quality management approach.
- (b) In general, we believe that the proposals generate benefits for engagement quality. We have concern as to whether there is enough guidance provided to establish a strong culture at the firm level to have a focus on quality management. We recommend expanding the guidance in the governance and leadership section.
- (c) We believe that the requirements and application material of proposed ED-ISQM 1 are scalable in that all practitioners will be guided through the same exercise and thought process. The results and documentation will vary based on size, complexity and circumstances.

There are challenges for smaller firms in the areas of monitoring and remediation and challenges for resources to mitigate risks. The sole practitioner must have professional skepticism already ingrained as no examples or boilerplate documentation guidance will overcome the issue.

We believe it would be helpful to clarify the documentation expectations and to provide more examples. If there were an opportunity to -specify some types of risks for all practitioners to consider, that would improve the scalability of the standard, especially for smaller firms and sole practitioners.

## **Request for Comment 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 noted in response to Request for Comment 1(c), smaller firms and sole practitioners could face challenges in the areas of monitoring and remediation as well as in finding resources to mitigate risks.

Implementation guidance with examples focused towards the smaller firm and sole practitioner will be critical. The implementation guidance will also help regulators understand how the standard is to be applied.

**Request for Comment 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?*

Please see previous comments on the need for additional examples.

The additional examples and explanations should focus on the size and complexity of the engagements being performed as well as the size and complexity of the firm. The client base of the firm should be considered as part of the required documentation to demonstrate competency and experience in industries and fields.

**Specific Questions**

**Request for Comment 4:**

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

Overall, we are supportive of the eight components and the structure of the ED-ISQM 1. However, we believe that the firm's risk assessment process should be applied to the other components of the system of quality management. The risk assessment process should include governance and leadership.

**Request for Comment 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.

While the objective connects the system of quality management to providing reasonable assurance that the firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, there is no direct linkage to public interest. "Public interest" should be defined.

**Request for Comment 6:**

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

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

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

*i. Are the required quality objectives appropriate?*

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

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

*(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?*

*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?*

(a) As we noted in a previous comment, we believe that the firm's risk assessment process should be applied to the other components of the system of quality management. The risk assessment process should include governance and leadership.

(b)(i) We found the definition of "quality objectives" in Paragraph 19(p) to be circular. We recommend the definition of "quality objectives" as the objectives that, when achieved by the firm, collectively provide the firm with reasonable assurance that the objectives of the system of quality management as defined in Paragraph 19(v) have been achieved.

(b)(ii) Yes, we believe that ED-ISQM 1 is clear that there are quality objectives beyond those required. However, implementation guidance and examples would be helpful in this area.

(c) Yes, we support the process for the identification and assessment of quality risks. Again, implementation guidance and examples would be helpful. We also recommend the concept of "reasonable possibility" be included in Paragraph 28(b) such that "if they were

to occur or may have a reasonable possibility of occurring, may individually or in connection with other quality risks, have a significant effect on the achievement of a quality objective(s).”

- (d)(i) We support the approach that requires the firm to design and implement responses to address the assessed quality risks. We recommend a revision in the last sentence of Paragraph 10(c) to refer to the sufficiency of responses as “may not” instead of “will not” such that “the responses required by this ISQM alone may not be sufficient to address all of the firm’s assessed quality risks...”
- (d)(ii) While the responses required by the ED-ISQM 1 are clear, we do not believe that the required responses have been appropriately connected to the quality risks. Additional guidance in this area would be helpful.

**Request for Comment 7:**

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

Yes, we believe that the revisions to the standard appropriately address firm governance and the responsibilities of firm leadership.

**Request for Comment 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?*

- (a) Yes, we believe that the ED-ISQM 1 should require firms to assign responsibility for relevant ethical requirements to an individual or individuals in a firm. We also believe that the firm should be required to assign responsibility for compliance with independence requirements to an individual or individuals.
- (b) Yes, we believe that the standard appropriately addresses the responsibilities of the firm regarding the independence of other firms or persons within the network.

**Request for Comment 9:**

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

Yes, we believe that the ED-ISQM 1 has been appropriately modernized to address the use of technology and that the technology terminology is broad enough so that the wording is not likely to become outdated.

**Request for Comment 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 transparency report or otherwise, when it is appropriate to do so?*

We believe that the requirements for communication with external parties may result in valuable and insightful information. However, we are concerned whether there is sufficient guidance provided to result in balanced reporting of the firm's quality management system. Paragraphs 40(e) and 41(c) permits reporting "as the firm deems appropriate." Reports and communications on the system of quality management should not be misleading.

Paragraph A150 provides examples of what the communication with external parties may contain. We recommend that the guidance include linkage to ethical requirements and that the communication with external parties be subject to the guidance in the IESBA Code of Ethics.

As to whether the proposals encourage firms to communicate via transparency report or otherwise, we believe that the proposals encourage communication with external parties about the firm's system of quality management, but question whether the proposals imply that smaller firms should be preparing a transparency report. The implementation guide should include examples of appropriate communications as an alternative to a transparency report.

Paragraph A147 provides an example for a firm that only performs compilation engagements and states that external parties may obtain information about the firm's system of quality management through discussions and direct interaction with the firm. It would be helpful for the implementation guide to provide more direction on the envisioned extent of the communication for these types of situations.

**Request for Comment 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?*

We have concern that the requirements as currently stated in the proposals could lead to inconsistencies and pose a regulatory challenge. Paragraph 37 (e)(ii) states that an engagement quality review is required for audits of financial statements of entities that the firm determines are of significant public interest. As noted in a previous comment, “public interest” has not been defined in the proposals. This requirement will be difficult to apply consistently in practice and difficult to regulate absent such a definition..

**Request for Comment 12:**

*In your view, will the proposals for monitoring and remediation improve the robustness of firms’ monitoring and remediation? In particular:*

- (a) Will the proposals improve firms’ monitoring of the system of quality management as a whole and promote more proactive and effective monitoring activities, including encouraging the development of innovative monitoring techniques?*
- (b) Do you agree with the IAASB’s conclusion to retain the requirement for the inspection of completed engagements for each engagement partner on a cyclical basis, with enhancements to improve the flexibility of the requirement and the focus on other types of reviews?*
- (c) Is the framework for evaluating findings and identifying deficiencies clear and do you support the definition of deficiencies?*
- (d) Do you agree with the new requirement for the firm to investigate the root cause of deficiencies? In particular:*
  - i. Is the nature, timing, and extent of the procedures to investigate the root cause sufficiently flexible?*
  - ii. Is the manner in which ED-ISQM 1 addresses positive findings, including addressing the root cause of positive findings, appropriate?*
- (e) Are there any challenges that may arise in fulfilling the requirement for the individual assigned ultimate responsibility and accountability for the system of quality management to evaluate at least annually whether the system of quality management provides reasonable assurance that the objectives of the system have been achieved?*

(a) Yes, we believe that the proposals could improve firms’ monitoring of the system of quality management as a whole and promote more proactive and effective monitoring. We would expect firms to explore the development of innovative monitoring techniques.

(b) Yes, we agree with the conclusion to retain the requirement for the inspection of completed engagements for each engagement partner on a cyclical basis.

- (c) Yes, we believe that the framework for evaluation findings and identifying deficiencies is clear and we support the definition of deficiencies.
- (d)(i) Yes, we believe that the nature, timing and extent of the procedures to investigate the root cause is sufficiently flexible.
- (d)(ii) Yes, we believe the manner in which ED-ISQM 1 addresses positive findings is appropriate.
- (e) We have not identified any foreseeable challenges that may arise in fulfilling the requirement for the individual assigned responsibility and accountability for the system of quality management to evaluate at least annually the system of quality management.

**Request for Comment 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?*

Yes, we support the proposals addressing networks.

We believe that ED-ISQM 1 is clear that the firm has the responsibility for quality management and not the network and that firms should not only rely on network requirements or network services.

**Request for Comment 14:**

*Do you support the proposals addressing service providers?*

Yes, we support the proposals addressing service providers.

**Request for Comment 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?*

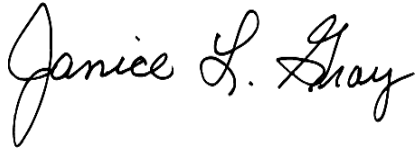
With respect to the state boards of accountancy as regulators of the profession in the United States, we do not believe that there would be significant difficulties in adopting at a jurisdictional level the change in title. However, there are state boards of accountancy that are required by other statutes to adopt only a named, dated version of a particular set of standards. These jurisdictions may face transition issues if they mandate compliance with a set of standards that no longer exists or only exists under a different name.

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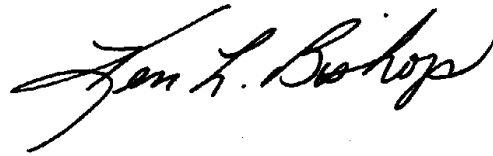


We appreciate the opportunity to comment on the Exposure Draft.

Very truly yours,

A handwritten signature in black ink that reads "Janice L. Gray". The signature is written in a cursive style with a large initial 'J'.

Janice L. Gray, CPA, CVA  
NASBA Chair

A handwritten signature in black ink that reads "Ken L. Bishop". The signature is written in a cursive style with a large initial 'K'.

Ken L. Bishop  
NASBA President and CEO