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The Quality Management Standards

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Panelists



Jeanne Viljoen

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Juané Schreuder

Juané Schreuder is an independent Audit Quality consultant and a past chairperson of the SAICA Assurance Guidance Committee.

She has extensive experience in training Chartered Accountants through various roles, which include Quality Control Manager and Training and Development officer with firms in Cape Town.



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Q1: What is the relationship of ISQM 1 with ISQM 2 and ISA 220 (Revised)?

ISQM 1 deals with the firm's responsibility for having a system of quality management. So, a system of quality management (SOQM) is the mechanism that creates an environment that enables and supports engagement teams in performing quality engagements – it helps the firm in achieving consistent quality engagements, as it focuses on how the firm manages the quality of engagements performed.

ISQM 1 requires a firm to design, implement and operate this SOQM to manage the quality of engagements by:

- Establishing quality objectives,
- Identifying and assessing the quality risk, and
- Designing and implementing responses.

Thus ISQM 1 manages the environment that enables and supports engagement teams to perform quality engagements.



Q1: What is the relationship of ISQM 1 with ISQM 2 and ISA 220 (Revised)? –cont.

ISQM 2 builds on ISQM 1 by providing specific requirements for:

- The appointment and eligibility of an engagement quality reviewer
- The performance of an engagement quality review; and
- The documentation of an engagement quality review.

ISQM 2 is designed to operate as part of the firm's SOQM, and therefore the requirements of ISQM 1 and ISQM 2 are organised in a manner that provide appropriate linkages between the standards.

ISA 220 (Revised) deals with the responsibilities of the auditor regarding quality management at the engagement level and provides requirements regarding the responsibilities of the engagement partner and team.

It is important to note that this standard **ONLY** applies to audits of financial statements.



Q2: To which firms/engagements do ISQM 1, ISQM 2 and ISA 220 (Revised) apply?

I think we all realise that these standards apply to firms that provide audit services, with ISA 220(R) being specifically applicable to audits.

Most of us would also agree that the ISQM standards would also apply to firms providing independent reviews.

What is critical for all accounting firms to realise, however, is that if a firm provides any of the following services, then the new ISQM standards will be applicable to the firm. It is therefore possible that a firm may not even provide audit or review services yet has to comply with these new ISQM standards.



Q2: To which firms/engagements do ISQM 1, ISQM 2 and ISA 220 (Revised) apply? –cont.

The services that are subject to ISQM 1 and ISQM 2 include:

1. Audits of historical financial statements where these audits are performed in terms of the International Standards on Auditing (ISAs 200 – 899)
2. Independent Reviews performed in terms of International Standards on Review Engagements (ISRE 2000 – 2699)
 - This service line includes both independent reviews of annual financial statements as well as the auditor's review of interim financial information
3. Assurance engagements other than audits or reviews of historical financial information (ISAE 3000 – 3699) are also included.
 - An example of this type of engagement is the audit of legal practitioner trust accounts
4. Lastly the so-called 'related services engagements' performed under International Standards on Related Services (ISRSs 4000-4699). These include
 - Compilation engagements
 - Agreed upon procedures engagements (often referred to as 'factual findings' reports)



Q2: To which firms/engagements do ISQM 1, ISQM 2 and ISA 220 (Revised) apply? –cont.

Where a firm performs other services, not mentioned earlier, ISQM 1 does not require that the system of quality management extend to those services. Some examples of these 'other services' are tax or consulting services.

Having said that, the firm's system of quality management will affect all areas of the firm, which will in turn affect other engagements and staff in the firm who are not involved in performing the audits, reviews and related services. The reason for that is simply that ISQM 1 promotes integrating quality management into the firm's culture, strategy, operational activities and business processes.



Q2: To which firms/engagements do ISQM 1, ISQM 2 and ISA 220 (Revised) apply? –cont.

Some examples of how other areas of the firm may be affected include:

- ISQM 1 requires the firm to establish a quality objective that 'The firm demonstrates a commitment to quality through a culture that exists throughout the firm. This requirement further requires the need for the firm's culture to recognise and reinforce the importance of quality in the firm's strategic decisions and actions, including the firm's financial and operational priorities'.
- ISQM 1 addresses human resources and technological resources. The firm's IT and HR functions may therefore be affected by the firm's system of quality management.
- ISQM 1 addresses resource needs and planning, including obtaining, allocating and assigning resources. This affects how resources, including financial resources, are allocated and utilised in the firm.
- ISQM 1 addresses the fulfilment of relevant ethical requirements. The firm may therefore need to design and implement policies and procedures that prohibit the provision of certain non-assurance services to clients that are public interest entities, where the firm performs audits or reviews of the clients' financial statements. It could also require the firm to design and implement policies and procedures that prohibit personnel from holding certain financial interests in entities for which such engagements are performed.



Q2: To which firms/engagements do ISQM 1, ISQM 2 and ISA 220 (Revised) apply? –cont.

In the case of ISQM 2, the standard will be applicable whenever an engagement quality review is required.

Historically, this was mostly only a requirement for audits of listed entities.

ISQM 1 now extends the scope of engagements requiring engagement quality reviews. The firm is therefore required to establish policies and procedures that address when an engagement quality review will be required for the following instances:

1. Audits of financial statements of listed entities
2. Audits or other engagements for which an engagement quality review is required by law or regulation
3. (and lastly) for audits or other engagements for which the firm determines that an engagement quality review is an appropriate response to address one or more quality risk(s).



Q2: To which firms/engagements do ISQM 1, ISQM 2 and ISA 220 (Revised) apply? –cont.

ISQM 1 expands on the last two categories by providing examples of when the engagement quality reviews may be required.

For example, Law or regulation may require an engagement quality review for audits of entities that are considered to be public interest entities, as defined in a particular jurisdiction. Another option could be to consider entities that operate in certain industries, such as Banks, Insurance companies or Pension Funds.



Q3: Is ISQM 1 scalable for smaller and less complex firms?

This is a very important question, especially in the context of the current Exposure Draft on the ISA for Less Complex Entities as well as the IAASB CUSP project (Complexity, Understandability, Scalability and Proportionality).

ISQM 1 requires a firm to tailor the design, implementation and operation of its SOQM based on the nature and circumstances of the firm and the engagements it performs. So the requirement is to customise the SOQM based on an individual firm.

HOW? The firm needs to exercise professional judgment when designing, implementing and operating the SOQM.



Q3: Is ISQM 1 scalable for smaller and less complex firms? –cont.

For example: Smaller and less complex firms are likely to have different quality risks than their larger counterparts thereby requiring a different response. For quality risks that are common across all firms of varying sizes and complexity, the nature, timing and extent of the responses may differ given the circumstances of the firm.

ISQM 1 contains application material with scalability examples. The ISQM 1 first time Implementation Guide also contains examples and material to consider for less complex entities.

ISA 220 (Revised) is also scalable by the way.

Q4: With just over a year to go, in which ways can firms implement these new standards?

Firstly, it is important to note that where a firm currently complies with ISQC 1, the firm will already have policies and procedures in place. Some of these policies and procedures may still be relevant and appropriate for the firm's new system of quality management, while others may need to be revised or enhanced in order to be compliant with ISQM 1.

In terms of how to go about implementation, there are a few options for firms.



Q4: With just over a year to go, in which ways can firms implement these new standards? –cont.

One option is to design the firm's system of quality management and to commence the operation of **all new and revised policies and procedures at the effective date**. This would therefore involve one big roll-out and implementation of the system of quality management. This option would give the firm more time to continue operating as it had up to now and have a big change to policies and procedures, all in one go, on the effective date.



Q4: With just over a year to go, in which ways can firms implement these new standards? –cont.

A firm may also decide to take a **phased approach** towards implementation, which then builds up to the effective date.

This may entail designing and implementing policies or procedures for only certain components of the system at a given time. The commencement of the operation of the policies or procedures will then be at various stages before the effective date. Let's say, for example, that a firm starts developing the firm's Risk Assessment process first, then moves on to the firm's Governance and Leadership etc. until all eight components have been addressed and the related policies and procedures are designed, implemented and operational.

The benefits to such an approach are that it may lessen the impact of too many changes all at once, giving everyone an opportunity to come to grips with the requirements of each additional phased roll-out.

When taking a phased-approach it is important to note that, although the firm would have implemented policies and procedures before the effective date, the firm would not be considered to have 'early adopted' ISQM 1 because only a portion of the system of quality management has been implemented before the effective date.



Q4: With just over a year to go, in which ways can firms implement these new standards? –cont.

Another option, possibly in combination with the previously mentioned options, is that the firm can also **pilot** or test the new system of quality management before the effective date.

This pilot or testing, may be on certain areas of the system of quality management, or by a selection of engagement teams.

The system of quality management would not be considered to be in operation until the firm has formally implemented and commenced operation of the new system of quality management in its entirety.



Q5: Who is responsible for the system of quality management?

Another very important question.

Paragraph 19 of ISQM 1 indicates that the firm is required to design, implement and operate a SOQM – thus the firm remains ultimately responsible for the SOQM. But a firm is not an individual that can take action, so ISQM 1 requires a firm to assign responsibilities for the SOQM AND the other aspects of the SOQM to individuals. These individuals are then held accountable for their assigned roles.

So what roles and responsibilities need to be assigned to individuals?

Q5: Who is responsible for the system of quality management? – cont.

- 1) Ultimate responsibility and accountability of the SOQM** – this is assigned to either the CEO or, if appropriate, the managing board of partners (or equivalent)
 - a. The person / persons are expected to have an understanding of ISQM1
 - b. Take ultimate responsibility and accountability of the firm to achieving the objective of ISQM 1, and
 - c. Is responsible for evaluating and concluding on whether the SOQM is achieving the objectives of the SOQM which is important to holding them directly responsible and accountable for the SOQM
- 2) Operational responsibility of the SOQM**
 - a. Also have an understanding of ISQM 1; and
 - b. Responsible and accountable for the design, implementation, and operation of the SOQM
- 3) Operational responsibility of specific aspects of the SOQM**
 - a. Compliance with independence requirements
 - b. Monitoring and remediation process (overseeing monitoring and remediation, and to take actions related to the remediation of deficiencies and communicate matters related to monitoring and remediation)
 - c. Other aspects as identified by the firm.



Q5: Who is responsible for the system of quality management? –cont.

What is very important is that individuals assigned these responsibilities are required to have the appropriate experience, knowledge, time, influence and authority! Also that the individuals assigned responsibility have a direct line of communication to the individual(s) assigned ultimate responsibility and accountability for the system of quality management.

Application material in the standard provides examples of:

- How to assign roles and responsibilities and
- How the firm is responsible for the evaluation and conclusion on the SOQM and further assigns the evaluation and conclusion to the individuals with ultimate responsibility and accountability for the SOQM.

Implementation Guides: References

Q1: ISQM 1: Page 6

Q2: ISQM 1: Page 4 & ISQM 2: Page 7

Q3: ISQM 1: Pages 12, 30, 51, 98

Q4: ISQM 1: Page 7

Q5: ISQM 1: Page 14



In need of more info?

Please visit our website at:

<https://www.saica.org.za/resources/audit-and-assurance/technical-resource/the-quality-management-standards>



Thank you and all the best with your implementation



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