

Private & Confidential

Ms K Dalby
Project Director
Financial Reporting Council
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Date: 11/03/21

Dear Kate

Proposal to adopt ISQM (UK) 1 Quality Management For Firms That Perform Audits Or Reviews Of Financial Statements, Or Other Assurance Or Related Services Engagements, ISQM (UK) 2 Engagement Quality Reviews, and revise ISA (UK) 220 (Revised November 2019) Quality Control For An Audit Of Financial Statements

Mazars is an internationally integrated partnership, specialising in audit, accountancy, advisory and tax services. Operating in over 90 countries and territories around the world, we draw on the expertise of 40,400 professionals – 24,400 in Mazars' integrated partnership and 16,000 via the Mazars North America Alliance – to assist clients of all sizes at every stage in their development. In the UK, Mazars has around 140 partners and over 1,750 employees and is ranked one of the top 10 accountancy firms nationally.

We welcome the opportunity to provide comments on the FRC's proposal to adopt ISQM (UK) 1 and ISQM (UK) 2 and to revise ISA (UK) 220. We believe the standards will help improve quality in both firmwide procedures and in the way audits, reviews and other assurance related engagements are conducted and documented.

We attach our responses to the five questions asked in your consultation document, as well as some general comments which we trust are of assistance.

As part of our response and recognising the complexity of the changes these standards bring, we encourage the FRC to prepare supplementary materials outside of the standards themselves. This may include example quality objectives and quality risks and building on the IAASB FAQ document with UK-specific content and guidance.

In addition, we have highlighted opportunities where we consider linkages can be made between the standards and other initiatives undertaken by the FRC in related areas and with wider education standards.

With kind regards

Yours sincerely



Jac Berry

Partner, Head of Quality

Q1. Do you agree that ISQM (UK) 1, ISQM (UK) 2, and the revised ISA (UK) 220 should be adopted in the UK, alongside the related conforming amendments to other ISAs (UK)? If not, please give your reasons.

We agree that the package of standards and related conforming amendments to other ISAs (UK) should be adopted in the UK. It is important that the UK continues to be at the forefront of international developments.

We support the overall change in focus from quality control to quality management brought about by these standards. This promotes a proactive, dynamic, and risk-based approach to quality which is customised to a firm and its engagement portfolio in an evolving environment.

Mazars is a member of the IFAC Forum of Firms and supports fully the initiatives of IFAC, IAASB, IESBA, Forum of Firms and Transnational Auditors Committee, as well as regulators such as the FRC and the ICAEW in areas of common interest. We are committed to supporting and applying those initiatives.

As a firm which is part of an international and integrated partnership, we share the FRC's support for the international harmonisation of auditing standards based on ISAs. For that reason, we agree with the FRC's decision to not propose significant supplementary material to the UK standards compared to the final international standards issued by the IAASB.

Notwithstanding this, in our response to Q2 below we have suggested additions to ISQM (UK) 1 and ISA (UK) 220 revised to provide clearer linkages with other standards and initiatives already in place or communicated, and additional guidance in some areas.

Q0. If you agree that the ISQMs (UK) and ISAs (UK) should be revised to adopt the revisions to the underlying international standards, do you agree that the proposed UK supplementary material is appropriate? If not, please give your reasons and explain what further additions or subtractions should be made

We note that the supplementary material proposed by the FRC is principally provisions required by UK legislation and regulation and to maintain equivalence with EU audit regulation. Accordingly, we agree that this material is appropriate.

Notwithstanding this, we have raised below some observations where we consider further additions or clarifications would be helpful.

Audit Quality Indicators

In May 2020, the FRC's Audit Quality Review team (AQR) issued a report on its findings from a thematic review on Audit Quality Indicators (AQIs). The findings were based on a benchmarking of AQIs monitored privately within the six largest UK audit firms.

As set out in that report, the FRC defines AQIs as "quantitative and qualitative measures of external audit quality, including both inputs and outputs. They indicate the firm's historical, present or future ability to perform quality audits, as well as providing insights into audit quality when read with other AQIs and relevant context".

One of the key findings made by AQR in its report was to consider the development of AQIs in the context of ISQM 1, namely **"firms should consider what AQIs they will need to monitor achievement of their quality objectives and include them in their AQI development plans"**.

The FRC has not currently included in ISQM (UK) 1 further references or explanatory material in relation to “indicators” to those made in ISQM 1, or otherwise referred to AQIs in ISQM (UK) 1.

In our view, this is an opportunity to make a clearer link between ISQM (UK) 1 and the AQR’s findings on AQIs. In particular, AQIs may be used as a tool for monitoring the effectiveness of systems of quality management by, for example, providing a measure of the achievement of quality objectives and, for specified firms, transparency on the effectiveness of systems of quality management through public reporting. Supplementary explanatory material could be added to ISQM (UK) 1 which draws on the other key findings made in the thematic review report issued by AQR.

We do not propose that such additional requirements or guidance be mandated for all firms in scope of ISQM (UK) 1 as we recognise the importance of scalability. In the same way, the scope of ISQM (UK) 1 is restricted in some areas (such as requirements specific to audits of public interest entities), requirements relating to AQIs could also be restricted to firms meeting specific criteria.

Evaluating the system of quality management

Paragraph 53 of ISQM (UK) 1 states that “the individual(s) assigned ultimate responsibility and accountability for the system of quality management shall evaluate...the system of quality management. The evaluation shall be undertaken as of a point in time, and performed at least annually” and, per paragraph 54, make a conclusion based on that evaluation. This is consistent with ISQM 1.

A system of quality management should be designed to avoid deficiencies from occurring but, when they do occur, having proper mechanisms in place to detect and then remediate in a timely manner.

Currently, ISQM (UK) 1 provides guidance on the importance of remediating deficiencies, in particular those which are pervasive and severe. However, since an evaluation under paragraph 53 is carried out at a point in time, there is a potential expectation gap over how to treat deficiencies identified near to the evaluation date. In particular, it is unclear what the FRC’s expectation is when a deficiency is detected very near to the date of evaluation under paragraph 53, but where such a deficiency has not been remediated as at the evaluation date.

When developing ISQM 1 the IAASB considered, among other risk management frameworks, the COSO Integrated Framework (2013). In the Q&A issued by COSO, it states that “regulators, standard-setting bodies, and other relevant third parties may establish criteria for defining the severity of, evaluating, and reporting internal control deficiencies”.

In view of this, and to ensure consistency, we would welcome supplementary guidance from the FRC on evaluating a system of quality management which takes account of these matters.

Competence and capabilities

Paragraph 32 of ISQM (UK) 1 requires a firm’s personnel to be “hired, developed and retained and have the competence and capabilities to consistently perform quality engagements, including having knowledge or experience relevant to the engagements the firm performs”.

The associated application and other explanatory material in paragraph A89 refer to “law, regulation, or other professional standards” which “may establish requirements addressing competence and capabilities, such as requirements for the professional licensing of engagement partners”.

ISQM (UK) 1 refers separately to engagement partners in paragraph A89. We recommend adding here an explicit reference to International Education Standard 8, Professional Competence for Engagement Partners Responsible for Audits of Financial Statements (Revised) (IES 8), as issued by the IAESB. This would promote consideration of interrelationships between auditing and education standards in a firm’s system of quality management. References to the extant ISA 220 and ISQC 1 are made in IES 8, and it would be consistent to include references to IES 8 in ISQM (UK) 1.

In addition, we recommend adding a reference to IES 8 in the associated application and other explanatory material to paragraph 40 of ISA (UK) 220. IES 8 sets out the competencies required for engagement partners responsible for audits of financial statements. It is appropriate for an engagement partner to consider these competencies when determining that their involvement has been sufficient and appropriate throughout the audit engagement.

Further, while we have every confidence in each of our engagement partners to undertake, in good faith, the self-evaluation required by paragraph 40 of ISA (UK) 220, there is a risk of bias inherent in conducting such self-evaluations. To promote the effectiveness of this exercise, we would welcome additional guidance from the FRC, either within or outside ISA (UK) 220, on how to ensure consistency between engagement partners and how to promote an impartial assessment.

Additional guidance and examples

To avoid discrepancies in understanding between firms, we would welcome additional supplementary guidance, outside of ISQM (UK) 1, in the form of examples in the following areas:

- Quality objectives;
- Quality risks;
- Quality indicators; and
- How to evaluate deficiencies.

Q3. Is the proposed effective date, which is consistent with the effective date of the IAASB's revised ISQMs and ISAs, appropriate? If not, please give reasons and indicate the effective date that you would consider appropriate.

We support an effective date of ISQM (UK) 1, ISQM (UK) 2 and the revised ISA (UK) 220 which is consistent with the effective date of the international standards issued by the IAASB.

While noting the FRC's preference for a shorter implementation period of 18 months, first implementation of the standards will incur significant developments and changes to systems, additional resources, training, and potential enhancements to culture and behaviours if it is to be done effectively.

Given the important changes brought about by the new standards, it is essential that sufficient time be given for firms to design and implement systems and processes which are effective and robust, with time to test such systems and processes before they are live.

Further, as the standards apply to all firms which carry out audits or reviews of financial statements, or other assurance or related services engagements, an implementation period of 24 months provides flexibility to those firms with more limited resources, which may need to engage external providers to assist in their development of a system of quality management.

We therefore support an implementation period of 24 months, while noting the FRC's strong encouragement for early adoption.

Q4. ISQM (UK) 1 requires the auditor to establish a monitoring and remediation process that identifies, evaluates and responds to findings that result in one or more deficiencies in the firm’s system of quality management. Do you agree with this approach or should the standard include requirements for firms also identify, evaluate and respond to positive outcomes and opportunities? Please give reasons for your response.

While we understand the value of identifying positive outcomes and opportunities, which we endeavour to do as part of our internal quality monitoring activities, requiring firms to identify, evaluate and respond to positive outcomes and opportunities is not considered appropriate at this stage.

The term “quality engagement” is used 14 times in ISQM (UK) 1 but is not defined explicitly. We interpret a “quality engagement” as one which complies fully with applicable law, regulation, and standards, with ISQM (UK) 1 envisaging that a firm design, implement, and operate a system of quality management which meets the objective of delivering quality engagements consistently.

Fundamental to an effective risk management framework (and in the context of ISQM (UK) 1, a system of quality management) is the premise that such a system is designed and implemented, from the outset, to deliver quality engagements consistently. As part of this, the system of quality management should have controls in place which are designed and implemented to detect and remediate deficiencies in a timely manner, thereby ensuring that the system of quality management is operating effectively to achieve the stated objectives.

Absent a deficiency in a system of quality management, it follows that the system of quality management is delivering quality engagements consistently. In such cases, positive outcomes and opportunities, while useful, do not of themselves necessarily contribute further to that system’s effectiveness. In other words, a quality engagement cannot be of a “higher” quality to another quality engagement if both are complying fully with applicable law, regulation, and standards.

We instead view positive outcomes and opportunities as one of several ways to remediate deficiencies.

Accordingly, we support the wording proposed in ISQM (UK) 1, specifically paragraph A158, which links positive outcomes and opportunities to the activity of understanding and remediating deficiencies identified.

In addition, some firms carrying out audits or reviews of financial statements or other assurance or related services engagements may only undertake a limited number over a year. In our view, it would be inconsistent with paragraph 10 of ISQM (UK) 1, which sets out the scalability of the standard, to require such firms to identify, evaluate and respond to positive outcomes and opportunities when their evidence base is limited to relatively few engagements.

We therefore support the flexibility afforded currently by ISQM (UK) 1, where firms are encouraged to evaluate and respond to positive outcomes and opportunities where they are identified, but not being required to do so.

If the FRC decides to require firms to also identify, evaluate and respond to positive outcomes and opportunities, there would need to be a clear definition in ISQM (UK) 1 of “positive outcome” and “positive opportunity”, in the same way “deficiency” is defined, to ensure understanding and consistency across firms.

Q5. The requirements in ISQM (UK) 2 are currently applicable to all engagements for which an engagement quality review is required to be performed. Do you believe that ISQM 2 could be enhanced through further requirements and/or application material for non-assurance engagements? If so, please give your detailed reasons and explain how ISQM (UK) 2 could be enhanced, in the context of a non-assurance engagement.

In response to this question we understand, after reading paragraph 17 of the FRC's Consultation Paper and Impact Assessment, that reference here to "non-assurance engagement" should be "non-audit assurance engagement", being those non-audit assurance engagements in scope of the proposed ISQM (UK) 2.

We do not consider that ISQM (UK) 2 requires further requirements and/ or application material for those non-audit engagements in scope of the standard. In our view, the requirements and application material of ISQM (UK) 2 are written in a way that allows application across a range of audit and non-audit assurance engagements.

Other comments on the drafting of ISQM (UK) 1, ISQM (UK) 2 and revised ISA (UK) 220

We take this opportunity to raise additional matters outside the questions raised in the consultation:

- We would encourage the FRC to include a table of content in the final, published versions to aid navigation and readability.
- We note the following typographical errors:
 - ISQM (UK) 1 - paragraphs 16(p) and 35-1 refer to ISQC (UK) 1 and ISQC (UK), respectively; and
 - Para 34-1(h) cross refers to Para 52-1(b) which does not exist.
- While we recognise the specific complexity with regards to ISQM (UK) 1, in future consultations on revisions made to an auditing or ethical standard, we encourage the FRC to:
 - Publish a tracked changes version of the proposed standard to show clearly what has changed between the extant standard and the revised standard.
 - In circumstances where the FRC is adapting an international standard for UK purposes, publish a tracked changes version of the proposed UK standard to show clearly what changes have been made to the international standard.
 - Publish a tracked changes version of the final standard to show clearly what has changed when compared to the draft standard which was subject to consultation.