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August 31, 2021

Auditing Standards Board
American Institute of Certified Public Accountants
1345 Avenue of the Americas, 27th Floor
New York, NY 10019

Via Email to CommentLetters@aicpa-cima.com

Re: Proposed Statements on Quality Management Standards – Quality Management, *A Firm’s System of Quality Management and Engagement Quality Reviews*, and Proposed Statement on Auditing Standards, *Quality Management for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards*

Dear Board members and staff:

Grant Thornton LLP appreciates the opportunity to comment on Proposed Statements on Quality Management Standards – Quality Management (SQMS), *A Firm’s System of Quality Management and Engagement Quality Reviews*, and Proposed Statement on Auditing Standards (SAS), *Quality Management for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards*. We respectfully submit our responses to the requests for comment listed in the exposure draft and certain other comments for the Board’s consideration.

Overall, we support the development of a suite of quality management standards that is consistent with international standards. We see this as a positive step toward improving the quality of firms’ systems of quality management, leading to higher quality engagements performed by firms here in the United States. However, we do have several concerns, highlighted below, which we elaborate on further in our detailed responses provided in the Appendix.

Definitions

'Engagement team'

We are concerned with the proposed definition of “engagement team.” It is our understanding that the proposed definition of engagement team would include component auditors, which we believe could lead to a variety of operational challenges when applying certain requirements. In particular, we are concerned with the clarity of the requirements, as well as how such requirements would be applied, related to intellectual and technological resources in the context of component auditors some of whom are both engagement team members and service providers. Likewise, we are concerned with the appropriate application of quality management at the engagement level and the extent of the engagement partner’s responsibilities, such as taking responsibility for consultations being undertaken by component auditors and determining that sufficient and appropriate resources are made available to component auditors. While we appreciate some of the additional application guidance that has been added beyond international standards, the requirements themselves are not clear on their own.

We understand that the IAASB intends to address the various concerns raised regarding the application of the proposed quality management requirements to component auditors as part of its group audits project. As a result, we encourage ASB members to consider whether waiting for the IAASB to make further progress on its group audits project might help clarify how to apply the proposed quality management standards and requirements at the engagement level. We note, however, that international standards do not allow engagement teams to make reference to a component auditor in the auditor’s report. Accordingly, we believe the ASB needs to decide whether component auditors, when the group auditor makes reference, are in fact members of the engagement team and, based on that conclusion, determine whether additional guidance is necessary. We further believe it is vital that the AICPA’s Professional Ethics Executive Committee (PEEC) deliberate, conclude, and provide guidance on the related independence ramifications of including component auditors as members of the engagement team prior to adopting the proposed definition. We do not believe that the independence requirements apply equally to firms and engagement team members who are component auditors.

In addition, an incorrect interpretation of what constitutes a “procedure” in this definition could result in diversity in practice and the misapplication of the proposed requirements, such that additional guidance may be warranted. For example, which aspects of an external confirmation constitute the procedure?

Absent further clarity of these issues, we believe the proposed definition may have unintended consequences on who is considered a member of the engagement team as well as on the procedures that are required for those individuals. This includes situations that are described in the group audits standard where an auditor may use the work of another auditor (other auditor) that is not a component auditor.

'Auditor'

To address potential unintended legal consequences arising from network firms and other firms comprising an engagement team under the proposed definition, we suggest that the Board consult with legal counsel as to the proposed change in the definition of engagement team as well as whether there is a need to modify the definition of an "auditor" in the Glossary of Terms in US GAAS. As currently defined, the term "auditor" includes members of the engagement team. With the proposed definition of engagement team, the Board would include component auditors (or other auditors) within the firm's network and other firms in the proposed definition of auditor. However, references to an "auditor" throughout generally accepted auditing standards (GAAS) have been made historically in the context of the firm and the related engagement team issuing the auditor's report. Therefore, it might be inappropriate to imply that references to "auditor" throughout GAAS now also include component auditors (or other auditors), as this interpretation could considerably blur the lines of responsibility. In this regard, the definition of "auditor" could be enhanced or clarified to refer to or acknowledge the auditor of the group financial statements.

'Deficiency'

We also have concerns about the proposed definition of "deficiency in the firm's system of quality management" (deficiency) and how this term is intended to interact with the definition of "deficiency" as it appears in paragraph 70b of Standards for Performing & Reporting on Peer Reviews (PRS). The inconsistency in definitions could lead firms to draw different conclusions in evaluating their systems of quality management and in peer reviewers' evaluation of such systems. We believe this is a matter to be further discussed with the Peer Review Board (PRB), and we encourage the AICPA to develop guidance for firms and peer reviewers to enhance the understandability and consistency of the terms used. This may further include understanding the PRB's plans, if any, to revise the PRS and collaborating on key definitions or requirements.

We note that some of our comments concern differences that specifically relate to our jurisdiction. In this regard, we continue to encourage the Board to consider differences in our jurisdiction as part of their convergence and harmonization efforts with international standards.

Effective date

While we support the phased approach to the effective date, we are significantly concerned that the proposed effective date of 18 months from approval would not allow sufficient time for firms to properly implement and properly address the new requirements, particularly for those firms that might not operate globally or adopt international standards. The short implementation period might lead to policies and procedures being implemented that do not fully address the proposed new requirements and might impact audit quality in the short term.



We would be pleased to discuss our comments with you. If you have any questions, please contact Jeff Hughes, National Managing Partner of Audit Quality and Risk, 404-475-0130, Jeff.Hughes@us.gt.com.

Sincerely,

/s/ Grant Thornton LLP

Appendix

Responses to requests for comment and issues for consideration

Proposed SQMS No. 1

Question 1: Respondents are asked to provide their views on the preceding changes. In addition, the ASB is seeking respondents' views on whether the requirements in proposed SQMS No. 1 are clear and understandable and whether the application material is helpful in supporting the application of those requirements.

Overall, we are supportive of the new quality management approach. We believe that a proactive approach to managing quality will provide a sound foundation that creates an environment for improved engagement quality.

There are areas in proposed SQMS 1 where we feel that further guidance would be beneficial for firms in understanding the boundaries of the requirements, the level at which risks would be identified, the extent of the evidence firms would need to gather, and the documentation needed to comply with the standard. This is especially relevant in the areas of network requirements and service providers.

Further guidance would also be helpful in relation to the assignment of an individual responsible for performing an annual evaluation of the firm's system of quality management and, in particular, the level of information or documentation that the individual might review in order to make the evaluation.

We recognize that firms may identify and document risks at different levels. Our main concern is the judging of one firm based on another firm's practices and policies. It is possible that coordination with the PRB may alleviate the need for specific guidance within the proposed standards.

Components of the system of quality management

We support how SQMS 1 organizes a firm's system of quality management into components, given that the proposals also allow firms the flexibility to adapt those components, as necessary, to their own terminology and frameworks (proposed paragraph A3) and to undertake the risk assessment process for the system of quality management as a whole.

We recommend that the Board further emphasize that, irrespective of the terminology or framework used, a firm's system of quality management should be designed to incorporate all of the required quality objectives and quality responses set out in the proposed standard, to avoid potential noncompliance with the proposed standard if firms' frameworks are significantly different.

Objective of the proposed standard

We are supportive of the objective of the standard; however, see our response to question 2 below with respect to compilation and agreed-upon procedures engagements.

Risk assessment process

As our firm continues to work on the implementation of the international quality management standards, we have encountered some challenges with the risk assessment component. We believe the profession would greatly benefit from robust implementation guidance to assist practitioners in understanding the level of granularity that is expected in the documentation of this component. This guidance could include examples of how risk assessment may differ, regardless of the size of the firm. We believe this guidance could also assist with the risk of inconsistent application as well as our concern expressed above.

Application guidance would also be helpful in the area of documentation and, particularly, the nature and extent of documentation of the firm's rationale for the level at which the firm assessed its quality risks.

Governance and leadership

We generally support the revisions to the standard to address the responsibilities of firm leadership and do not have any recommended revisions to the proposed requirements.

Resources

We generally support the proposed requirements related to the Resources component. Further, we appreciate the guidance provided by proposed paragraph A115, which we believe clarifies the interplay of the requirements for service providers who are component auditors.

Information and communication

We generally support the proposed requirements related to the Information and Communication component. We believe further guidance may be needed for firms to understand the boundaries of the requirement, the extent of the evidence that firms need to gather, and the documentation needed to comply. We feel the lack of guidance is particularly apparent in proposed paragraph 34(d) from the perspective of communications with service providers. Practically speaking, we are struggling to identify communications that would be necessary to third parties or non-network firms on these topics in order for those resources to fulfill their responsibilities.

Monitoring and remediation

We believe that the proposed standard would improve firms' monitoring of their system of quality management as a whole and would promote more proactive and effective monitoring activities.

We agree with the incorporation of a new requirement to investigate the root cause of identified deficiencies and believe that the guidance allows for sufficient flexibility. We further support the inclusion of guidance that explains that the procedures undertaken to understand the root cause of an identified deficiency may be simple, considering the term "root cause analysis" is often associated with a complex, in-depth process. Further, we believe the application guidance added from International Standard on Quality Management (ISQM) 1 would be useful for firms in determining when they have performed sufficient analyses of the cause of the deficiency.

We note, however, that even firms that perform effective root cause analyses are unlikely to drive 100% quality firmwide. In other words, root cause analysis is good for identifying and addressing systemic quality issues across a firm, but it will not eliminate those "one off" deficiencies that result from human error. A firm's system of quality management provides reasonable, not absolute, assurance.

In addition, it is unclear to us when the evaluation of identified deficiencies is intended to occur. We question whether the Board intends for a deficiency to be evaluated once it is identified or if such evaluation is intended to coincide with the annual evaluation made by the individual at the firm who is ultimately responsible for the system of quality management. We ask the Board to consider adding application guidance to help clarify this timing question.

Networks

We understand the rationale for including requirements for using network firms and their services, and we agree that it is important not to place undue reliance on services and resources provided by the network in order to achieve quality. We are concerned, however, by the focus and the extent of the proposed guidance on networks.

We agree that the individual firm should be responsible for its own system of quality management, and we support the proposed standard addressing service providers. However, we do not agree with treating the network the same as a service provider. Unlike a service provider, a network shares the same reputation as the firms within the network and has a vested interest in promoting quality within the individual member firms. Arguably, the risks to quality are more extensive at firms that do not have access to the extensive resources a network can provide, yet the standard appears to be placing more of a burden on firms that participate in network resources.

The proposals require firms to understand the network requirements, network services and resources, and any responsibilities that the firm itself may have to implement when using those services and resources. The related application material provides examples of the types of inquiries and documentation that the firm may consider in performing its assessment, but it provides little or no guidance on the extent of that assessment or on the extent of the documentation required as evidence

that the firm has performed the assessment. We recommend that such guidance be incorporated into the proposed standard to guide firms in determining what systems or protocol they need to have in place to fulfill the requirements of the standard.

Paragraph-level observations and recommendations

We identified the following paragraph-level observations and recommendations for the Board's consideration:

- As described in greater detail in the body of our letter, we have concerns with the definitions listed below. We urge the Board to coordinate further with the PRB and with the Group Audits Task Force, as applicable, to address each matter:
 - Engagement team
 - Auditor
 - Deficiency in the firm's system of quality management.
- We note that there are various paragraphs throughout the proposal where the term "expert" or "experts" is used. We recommend those terms be updated to "specialist" or "specialists" in order to align with the language used in US GAAS.
- We recommend that the verb "shall" in paragraph 18 be changed to "should" in order to align with terminology used in US GAAS.
- We believe further guidance is necessary for the appropriate application of paragraph 48 of the proposed standard. Due to the operational challenges created by the proposed definition of "engagement team," it is unclear to what extent the matters are communicated to component auditors (or other auditors) who are either network firms or other firms. A literal application of this requirement could divulge sensitive, confidential, or privileged information to third parties that do not have a need to know such information. A firm's system of quality management addresses the use of network firms and services providers; network firms and services providers themselves are not part of a firm's system of quality management. We recommend adding language to this paragraph such as "to the extent relevant to their responsibilities" to avoid onerous and unnecessary communication expectations.

Question 2: Respondents are asked to provide their views on the scalability of the new quality management approach. In addition, the ASB seeks respondents' views on specific requirements in proposed SQMS No. 1 that may inhibit scalability and requirements for which additional application material regarding scalability would be helpful.

We believe that the standard is generally scalable for firms of varying sizes that perform audit, examination, and review engagements. However, the proposed requirements might be overwhelming for firms that perform only compilation or agreed-upon procedures engagements. We suggest that the Board consider whether all of the requirements are necessary for these types of firms or engagements. Further clarification of the extent of the assessment required for firms that form part of

a network where such firms only perform compilation or agreed-upon procedure engagements might also be helpful.

Proposed SQMS No. 2

Question 3: Respondents are asked to provide their views on the preceding changes. In addition, the ASB is seeking respondents' views on whether the requirements in proposed SQMS No. 2 are clear and understandable, and whether the application material is helpful in supporting the application of those requirements.

Separate standard

We support creating a separate standard for engagement quality (EQ) reviews as well as retaining the requirement in SQMS 1 for the firm to develop policies or procedures for engagements involving an EQ review. We believe that this approach promotes the scalability of the standards, so that when a firm determines that no engagement meets the criteria to require an EQ review, it is not required to address the requirements in SQMS 2.

We further support the proposed standard addressing the remaining aspects of the firm's system of quality management related to EQ reviews. By accumulating all the requirements relating to EQ reviews in a single and separate location, there is less opportunity for a requirement to be overlooked. Additional explanation and guidance can be provided without affecting the length and complexity of SQMS 1 or distorting the balance of EQ reviews relative to the other aspects of SQMS 1.

Nevertheless, we do have some concerns with the geography of this proposed standard and the implications for firms' implementation and subsequent evaluations, including conclusions related to deficiencies. We note that this proposed standard would no longer be part of US GAAS, which would be inconsistent with the PCAOB's equivalent standard that currently resides in auditing standards, not in quality control standards. This may create implementation challenges for firms with regard to how EQ reviews fall into, and interact with, a firm's overall system of quality management. In particular, guidance may be needed as to whether a departure from SQMS 2 might lead to a noncompliant engagement or to an issue with the firm's system of quality management. It is currently unclear because EQ reviews are engagement-specific, but the proposed standard governing them resides within the standards on quality management. We believe this is another point of possible coordination with the PRB.

Objective of the standard

As proposed, the standard's objective is unclear, particularly in light of our prior comment about EQ reviews no longer being part of US GAAS. We believe this standard essentially contains two objectives and, as drafted, does not sufficiently capture the two aspects of EQ review requirements contained within the proposed standard. There are requirements specific to the firm establishing its EQ review process, and there are differing requirements for EQ reviewers and for the actual execution and documentation of an EQ review. We believe separating the objectives into bullets would enhance the clarity of such objectives and better enable firms to ensure they have captured all aspects of the requirements in their systems of quality

management. In addition, a separate objective for the EQ reviewer would further clarify the EQ reviewer's responsibility to comply with the proposed standard.

Appointment and eligibility of reviewers

We are generally supportive of the proposed requirements regarding the eligibility of individuals to be appointed as an EQ reviewer or as an assistant to an EQ reviewer. While we appreciate that the standard deals with the authority, or perceived authority, of the EQ reviewer through the requirement in paragraph 18(a) and the related application material, experience indicates that difficulties can still arise when the EQ reviewer is of a grade lower than that of the engagement partner (or leader). We would therefore recommend that the application material provide further guidance on policies and procedures related to the notion of "sufficient authority," considering scalability for smaller firms.

In addition, we note that the application material, specifically paragraph A10, indicates that the authority of the EQ reviewer becomes diminished where the EQ reviewer has a reporting line to the engagement leader. This may not always be possible, and we recommend that the proposed standard include guidance that provides examples of the safeguards that a firm could put in place where it is not practical.

Paragraph 20 of proposed SQMS 2 allows for individuals to assist the EQ reviewer in the performance of the review. Firms might interpret the related example in the application material to mean that using assistants in the performance of an EQ review would be appropriate only in circumstances where specialized knowledge, skills, or expertise is needed in the execution of the review. We do not believe that this was the intention of the requirement and recommend that the Board revisit the guidance in this regard.

Further, we note that one of the factors to consider in the appointment of an EQ reviewer is whether the reviewer would have sufficient time to fulfill the role. The appointment of assistants to help the EQ reviewer in the performance of the review might be helpful in circumstances where there is a limited pool of available EQ reviewers from which to draw.

Performance and documentation of the EQ review

In principle, we agree that the EQ reviewer's evaluation of significant judgments includes evaluating the engagement team's exercise of professional skepticism, required by proposed paragraph 22(c)(i). However, professional skepticism is a state of mind and may not be evidenced by specific documentation, which in turn would make it difficult for the EQ reviewer to evaluate and demonstrate the evaluation performed as part of the EQ review. We urge the Board to consider further guidance in the standards in this area, both on how engagement teams evidence their exercise of professional skepticism (likely in proposed QM SAS) and how the EQ reviewer evidences the evaluation of the engagement team's exercise of professional skepticism.

As an aside, we note that this proposed standard refers to "exercising" professional skepticism while GAAS refers to "maintaining" or "applying" professional skepticism.

Consideration may need to be given as to the consistency of these phrases across standards issued by the ASB and ARSC.

Timing of the review

We support the proposed requirement for the EQ reviewer to perform EQ review procedures at appropriate points in time during the audit. This would allow for a more thorough review by the EQ reviewer and would afford the engagement team adequate time to respond appropriately to the EQ reviewer's questions and comments. Please also refer to our response to Question 9 below, which provides additional feedback with regard to the timing of EQ reviews.

Documentation

We agree with the enhanced documentation requirements and believe that these enhanced requirements reflect what many firms currently require engagement teams to include in the engagement file as evidence of the EQ review.

Paragraph-level observations and recommendations

We identified the following paragraph-level observations and recommendations for the Board's consideration:

- We recommend the Board revise paragraph 25(f) to refer to "audit engagements" as opposed to "audits of financial statements." The more general term would then encompass audits of internal control that are integrated with audits of financial statements and compliance audits. We do not believe it is the Board's intention to exclude these audits from the requirements.
- In the third bullet of paragraph A6, we ask the Board to clarify the language so that it more closely aligns with how specialists are defined in US GAAS.

Proposed QM SAS

Question 4: Respondents are asked to provide their views on the preceding changes. In addition, the ASB is seeking respondents' views on whether the requirements in the proposed QM SAS are clear and understandable, and whether the application material is helpful in supporting the application of those requirements.

We agree that to take overall responsibility for managing and achieving quality on the audit engagement, the involvement of the engagement partner needs to be both sufficient and appropriate. However, there is a level of prescription to these proposed requirements that is not consistent with a principles-based approach. We further believe there are areas where additional clarity is necessary in order to make the QM SAS sufficiently operational, particularly for group audits.

For example, we note that paragraph 13 of the QM SAS requires the engagement partner to determine that the engagement partner has taken overall responsibility for managing and achieving quality on the audit engagement. There is little guidance on how the engagement partner evidences the basis for the conclusion reached. We would recommend the incorporation of additional guidance on the documentation expected to demonstrate compliance with this requirement.

Group audits

We are concerned that the extent of the requirements and the resulting responsibilities that lay directly with the engagement partner could make this standard too onerous to apply to large single-entity engagements or large multinational engagements. We would recommend that the application of the requirements in these circumstances be considered as part of the QM SAS. While we appreciate that, from a group audit perspective, the IAASB and ASB have indicated that the responsibilities of the group engagement partner will be considered in their respective projects on group audits, there will probably be a period of time when QM SAS is effective, but the revisions to AU-C section 600 will still be in development. We are concerned that this would be detrimental to audit quality. As a result, if these requirements are to remain in a revised standard, we recommend that the ASB provide guidance on how to apply these requirements to large single-entity engagements or multinational engagements when the revised standard is approved. If these requirements are not considered as part of the QM SAS, we would recommend that the effective dates of the QM SAS and a revised AU-C section 600 be aligned.

Effective date

Question 5: Respondents are asked to provide their views on whether the effective dates are clear.

We believe that the effective dates would be clearer if they were presented in the context of “periods ending on or after” as opposed to “beginning on or after,” since the former is the dating convention generally used by the ASB for new standards.

Question 6: Respondents are asked to provide their views on whether an 18-month implementation period is appropriate. If that period is not appropriate, please explain why and what implementation period would be appropriate.

As described in the body of our letter, we support the phased approach to the effective date. While we understand the desire for the proposed standards to be implemented as soon as possible, we have significant concerns that the proposed effective date, which is 18 months after the proposals are approved, would not allow sufficient time for firms to properly implement the standards and to properly address the new requirements, particularly firms that might not operate globally or adopt international standards. The short implementation period might lead to policies and procedures being implemented that do not fully address the proposed requirements and might be detrimental to audit quality in the short term. Therefore, we believe a longer implementation period is necessary.

Based on our firm’s ongoing implementation of the ISQM standards, SQMS 1 would require the dedication of a significant number of resources to establish a risk assessment process. In addition, resources would be needed to update firms’ methodologies for the two other quality management standards that will become effective simultaneously. Many firms, regardless of size, would find it difficult to allocate additional resources and to commit the necessary time to simultaneously implement the proposed standards. If insufficient time is given for firms to implement SQMS 1 in particular, there is a risk that firms will take their existing system and make

only minor adjustments to map the existing processes to the new requirements, rather than taking the necessary time to redesign the existing system to align with the fundamentally revised standards.

Additionally, there are two other significant standards—SAS No. 143, *Auditing Accounting Estimates and Related Disclosures*, and SAS No. 145, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*—with effective dates of periods ending on or after December 15, 2023. For a number of firms, the same pool of resources will be responsible for implementing all of these standards, for incorporating them into firm methodology, and for developing accompanying training. For firms to implement changes for five standards, four of which would likely represent significant changes, practically simultaneously may actually have an adverse impact on audit quality. Therefore, we believe that the effective date of the standard should be no less than 24 months from its approval.

Issues for consideration

Question 7: Respondents are asked whether they agree that inspection of completed engagements by those involved in the engagements should be precluded in order to enhance audit quality. If not, please explain why and provide examples of safeguards that could lower the self-review threat to an acceptable level.

We agree with precluding individuals who are involved in the engagement from inspecting the completed engagement. Although this may exacerbate resource constraints at smaller firms, we believe such prohibition would enhance audit quality overall since it effectively eliminates the self-review threat.

Question 8: Respondents are asked for their views on whether a cooling-off period should be required before a former engagement partner can serve as an engagement quality reviewer on that engagement, and (a) if so, the appropriate length of required cooling-off period, or (b) if not, please explain why and provide examples of safeguards that could lower the objectivity threat to an acceptable level.

We support requiring a cooling-off period for former engagement partners. However, we are concerned about requiring a specific two-year cooling-off period without considering the scalability of this requirement or flexibility for smaller firms. We note that in AS 1220, *Engagement Quality Reviews*, the PCAOB provides an accommodation for smaller firms based on the exemption under Rule 2-01(c)(6)(ii) of Regulation S-X, which states the following:

Any accounting firm with less than five audit clients that are issuers (as defined in section 10A(f) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-1(f))) and less than ten partners shall be exempt from paragraph (c)(6)(i) of this section provided the Public Company Accounting Oversight Board conducts a review at least once every three years of each of the audit client engagements that would result in a lack of auditor independence under this paragraph.

Since peer review is required every three years, we recommend the Board consider a similar accommodation. Otherwise, we recommend application guidance indicating

that a cooling-off period of at least one year is generally appropriate. The application guidance could also discuss how firms may establish protocols that are reasonable for the nature of their practices.

Question 9: Respondents are asked for their views on whether the engagement quality review should be required to be completed before the report is dated, rather than before the report is released.

We agree that the dating of the report and report release coincide more frequently than in the past. We do not foresee significant changes in our practice that would result from these requirements. Therefore, we support the requirement that the engagement quality review should be completed before the report is dated. We further support the corresponding proposed amendments to AU-C sections 700 and 703 that connect the report dating requirements to the EQ review requirements in the proposed quality management standard. We ask the Board to consider whether similar guidance would be beneficial to the corresponding report dating requirements contained in the attestation standards and standards for accounting and review services.