

February 1, 2023

Ms. Phoebe Brown  
Office of the Secretary  
Public Company Accounting Oversight Board  
1666 K St, NW  
Washington, DC 20006-2803

Dear Secretary Brown and PCAOB Board Members:

Johnson Global Accountancy is pleased to submit its comments on the proposed standard QC 1000, *A Firm's System of Quality Control*.

Johnson Global Accountancy's mission is to be the most innovative and technically excellent advisory firm at the intersection of companies, auditors, and regulators, that improves investor decision-making confidence. We help firms interpret, respond, and comply with global auditing and financial reporting standards and regulatory requirements, including those standards set by the PCAOB. Our team of financial reporting quality advisors help prepare firms to perform high quality audits using innovative tools with a shared commitment to implementing effective policies, procedures, and controls. We also provide firms with integrated software and service solutions to help them comply with audit quality standards. To date, we have advised a variety of firms on the implementation of International Standard on Quality Management (ISQM) 1 and Statement on Quality Management Standards (SQMS) No. 1.

We serve a diverse group of audit firms ranging from single office firms to more complex regional firms and the top 20 firms. Consistent with themes in the proposal, we have seen that when audit firms invest in their system of quality management, audit quality improves.

Overall, we are supportive of the PCAOB's objective to enhance and strengthen a firm's QC system by proposing new quality standards to improve and promote audit quality. We have observed that firms with satisfactory remediation of QC deficiencies result in fewer audit failures during monitoring programs, this is in-line with certain key findings in your Staff White Paper, *The Impact of Quality Control System Remediation on Audit Performance and Financial Reporting Quality*.

We agree with the PCAOB's focus on quality risks. The ability to scale and tailor the proposal to the nature of a firm's practice is also important. The proposal modernizes the existing standards and brings consistency by incorporating the SEC Practice Section (SECPS) requirements.

We applaud the focus to build on the existing ISQM 1 and SQMS 1 standards. Also, incorporating root cause analysis and the related lessons learned, recognizes the important steps that firms have taken and shows the value this function contributes to building effective systems to support quality audits.

In supporting firms with their system of quality management, we have noted that regardless of complexity and size, firms deal with resource challenges. Our overarching concern is whether this proposal is operational for all PCAOB-registered firms, especially those that are not annually inspected.

We have carefully considered all the Board’s questions. Rather than address all 93 questions on an individual basis, we are providing our comments based on themes that, from our discussions and work with PCAOB-registered firms world-wide, are important to them as they evaluate the Board’s proposal.

### **Extent of Differences to Other Standards**

The proposed standard differs in several areas from ISQM 1 and SQMS 1. The differences arise from requirements, definitions, and general terms used. These differences will impose additional challenges on smaller firms with no discernable contribution to audit quality. In fact, we anticipate that these differences may detract from a firm’s focused efforts on the objectives of the proposal.

The PCAOB’s November 18, 2022 “Comparison of Proposed QC 1000 with ISQM 1 and SQMS 1” highlights differences amongst the standards across 97 pages. We expect that the differences highlighted will require firms with multi-jurisdictional compliance requirements (e.g. CSQM 1, ISQM 1, SQMS 1, and others) to have multiple systems or sub-systems in place, with mechanisms to track the varying similarities and differences between these jurisdictions. We question whether triggering these differences will contribute to firms improving their audit quality. We recommend that the Staff carefully consider how the management of these differences will affect resources of firms, particularly smaller firms. Part of that consideration should be whether differences, other than those that are due to legal frameworks, be kept to a minimum. The additional requirements and specificity of each requirement would best be served through practice aids or other explanatory material. A revised approach along these lines would also support scaling the requirements to varying sized practices.

### **System of Quality Control vs System of Quality Management**

The proposal defines the new standards collectively as the “system of quality control” rather than “system of quality management” as used by other standard setters and it is not clear why this distinction is introduced. Continuing to use the term “control” seems to imply that this proposal is an update to the existing standards, and all that is needed is some additional controls to comply.

Adopting a system of quality management points to a new “north star” where firms are encouraged to think differently about their practice. We believe that use of “management” is all encompassing and incorporates the concepts of the continuous audit quality improvement, the importance of viewing the system as an iterative process, and the interaction of all the processes that together culminate in performing quality audit work. This may be policies, procedures, or controls.

We propose removing this difference to encourage firms to take a fresh approach and think about the entire management system of their firm and how the individual controls, policies, and procedures interact. This different emphasis points to a new fundamental approach – identifying, assessing, and responding to risks.

### **Risk Assessment, Annual Assessment and Reporting**

We agree that firms need to assess their system on an ongoing basis to both detect and prevent deficiencies. Paragraph .20 of the proposed standard outlines the annual requirement for the risk assessment process and references Appendix B for further examples. We recommend clarifying whether all the examples cited are intended to be covered. The current presentation implies that those examples will serve as a checklist and may therefore, make it more challenging to scale the standard. We agree and

support providing additional guidance and examples and it would be helpful to illustrate how those examples might be scaled in different-sized practices.

In addition, we suggest providing firms with the option to select the assessment date that works best in their circumstances. This would allow them to align their assessment with (i) its evaluation of the system of quality management under other standard-setters; (ii) an individual firm's fiscal year-end, or (iii) other reasons appropriate to the firm's circumstances. The "busy season" for each firm differs based on the nature of their practice and this flexibility would enhance scaling options for all sized firms.

We believe the timing of the requirement to report the new Form QC in January would be onerous for smaller firms, and like the assessment, firms should be provided with the option to align this to what works best for their practice.

We encourage the PCAOB to explore and consider whether the concept of "continuous auditing" could be applicable here; this option could also reduce the bottleneck of reporting as of a point in time.

### **Roles and Responsibilities**

The proposal lays out detailed responsibilities for the overall system of QC including specific roles for operations, independence and ethics, monitoring and remediation, and other components as appropriate. The proposal notes that if a firm has co-principal CEOs, that the reference to "individual" applies to each co-principal. It is not clear if this also applies to the remaining roles listed. In addition, Section C, Roles and Responsibilities of the proposal doesn't sufficiently consider the management structure of smaller firms where the firm's CEO may not be an audit practitioner and may designate and rely on others within their organization to fulfill the requirements of their QC systems.

Many smaller firms have already designed their process to accord with ISQM 1 and SQMS 1. Those standards permit these roles to be filled by an individual or individuals. It would be helpful and more practical to clarify these requirements and we encourage focusing on clarity of responsibility vs restricting to a particular person(s) or role(s).

### **Major QC Deficiency**

Paragraph .78 of the proposed standard would require firms to evaluate unremediated QC deficiencies as of the evaluation date to determine whether major QC deficiencies exist. This is a significant difference from the requirements in other quality management standards that firms are currently implementing. Specifically, ISQM 1 and SQMS 1 does not have this additional classification of "Major QC Deficiency". While we agree that findings in a quality control system may have different levels of severity, we expect that this additional deficiency classification will redirect time and resources to analyzing the level of a deficiency instead of the important elements to remediate the deficiency such as root cause analysis and implementing timely changes to a firm's system.

In addition, this creates significant differences from ISQM 1 and SQMS 1 and it is not clear how deficiencies identified under each standard would be reconciled or reported. The Board indicated in the proposal that "there may be circumstances in which a firm would conclude under QC 1000 that its QC system was ineffective, but still view its QC system as providing reasonable assurance for purposes of other QC standards." This potential discrepancy in conclusions on effectiveness, for the same system of quality

management of a particular firm, will present challenges to stakeholders trying to understand, interpret, and make decisions based on the effectiveness of a firm's system.

### **Scaling**

The proposal provides several requirements as to how each element of the system should be implemented. We are concerned that these are not sufficiently scalable for smaller firms and recommend that the material be added to an appendix or made optional. We recommend the staff consider providing smaller firms (e.g. triennially-inspected firms with less than 100 issuers) the option to comply with ISQM 1 or SQMS 1 as an acceptable alternative to QC 1000, or requiring a scaled standard with application guidance.

### **Independence**

The proposal expands on the independence requirements in a granular manner. We propose these details be moved to an appendix, practice aid, or provided as additional guidance to help reduce differences between QC 1000 and other standard-setters.

As an example, ISQMS 1 requires that quality objectives include the independence and ethical requirements that apply to a firm's circumstances. This principles-based requirement would, therefore, also include SEC requirements where an engagement is subject to them.

### **Communication of Policies and Procedures**

Paragraph .55 notes the communication of the policies and procedures related to the operation of the firm's QC system and the performance of its engagements to firm personnel and other participants. It would be helpful to clarify, in additional guidance, whether the communication is required in narrative, flowchart or other form.

### **Resources Specified Quality Responses**

Paragraph .47 indicates that firms should design, implement, and maintain policies and procedures for the engagement partner, and commensurate with their responsibilities, others participating in an engagement to obtain and maintain the competence to fulfill their respective assigned engagement roles, including an understanding of eight factors. The paragraph provides a level of specificity that appears to create two issues: (1) the material listed in paragraph .47 (a) – (h) is included in several other sections within the proposal and creates differences with other standards (2) the material does not consider that the industry is evolving at a rapid pace and these items may not be applicable in the future. To enhance adaptability and comparability with other standards, we propose including these items in staff guidance or other supplementary information instead of the standard.

### **Outreach to Smaller Firms**

We expect that the compressed timeline for the comment process will result in less written responses from mid-market and smaller firms, and these are the registered firms that will be proportionally most affected by the important changes this standard will require. As such, we encourage the Board's staff to increase engagement with smaller firms to proactively gather input on the proposed standard.

We see several implementation challenges for firms, including those that have already implemented ISQM 1, in particular, given the length and complexity of the document. While the proposal indicates it is

scalable, the main thrust of the proposal appears to be directed at the largest firms. This leaves smaller firms with the challenge of having to interpret and scale the proposal to their circumstances. We also recommend adding references at the bottom of each section to highlight differences between ISQM 1 and SQMS 1 to help small firms implement and interpret the proposal. This would be particularly important where firms need to comply with all three standards.

We support the PCAOB's efforts to modernize these standards. We would be pleased to discuss our comments with you at your convenience. Please direct any questions to Jackson Johnson, President ([jjohnson@jgacpa.com](mailto:jjohnson@jgacpa.com)) or Joe Lynch, Managing Director ([jlynch@jgacpa.com](mailto:jlynch@jgacpa.com)). They may be reached at (702) 848-7084.

Sincerely,

A handwritten signature in black ink that reads "Johnson Global Accountancy". The signature is written in a cursive, flowing style.

Johnson Global Accountancy