JOHNSON GLOBAL®
Advisory

June 26, 2024

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Dear Secretary Countryman and SEC Commissioners:

Re: PCAOB-2024-02: Proposed Adoption of A Firm's System of Quality Control and other amendments to PCAOB Standards, Rules and Forms

Johnson Global Advisory is pleased to submit its comments on the PCAOB's proposed adoption of *A Firm's System of Quality Control and other amendments to PCAOB Standards, Rules, and Forms* (collectively, the "proposed rules").

Johnson Global Advisory'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 implement 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. We have seen that when audit firms invest in their system of quality management, audit quality improves.

Overall, we support and share the PCAOB's objective to enhance and strengthen a firm's quality control system by adopting updated quality standards to improve and promote audit 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 essential. The proposed rules modernize the existing standards and bring consistency by incorporating the SEC Practice Section (SECPS) requirements.

As we stated on February 1, 2023, in our comment letter to the PCAOB on the proposed standard (see copy attached), our overarching concern is whether this proposal is operational for all PCAOB-registered firms, especially those that are not annually inspected. This concern remains. We specifically request additional time for the firms to evaluate the implications for their practices, especially, for any changes from the original proposal. Our key comments are set out below.

1. Focus on adopting "one system of quality control"

We believe that investors and audit quality are best served by audit firms having "one system of quality control" - one system that allows for compliance with varying standards, rules and regulations. The International Auditing and Assurance Standards Board's ISQM 1 and the similar AICPA SQMS No.

1 serve that purpose. Each of these standards is in effect and requires firms to ensure that their quality management system provides reasonable assurance that audits are performed in accordance with the applicable standards and local laws and regulations. The PCAOB proposed rule differs in several areas from ISQM 1 and SQMS 1 and these differences will impose additional challenges and costs on smaller firms with no discernable contribution to audit quality. In fact, based on work with firms worldwide that have already implemented ISQM 1, we share their concerns that implementing yet an additional (or in many cases, a third) new standard intending to address the same objectives will distract limited firm resources away from continuous audit quality improvement. Instead, these resources will spend more time differentiating between and ensuring compliance over the multiple standards across multiple jurisdictions. We continue to encourage the Board to reduce the differences with ISQM 1 and SQMS 1. The additional requirements and specificity that the PCAOB seeks through introducing these differences could be more effectively achieved through practice aids or other explanatory materials.

2. **Clarify definition of other professionals or organizations that the firm uses in connection with the firm's system of quality control**

   The standard defines "other participants" as "accounting firms (foreign or domestic, registered or unregistered), accountants, and other professionals or organizations, other than firm personnel, whose responsibilities include assisting with the performance of the firm's engagements or the design, implementation, or operation of the firm's QC system, including engagement quality reviews." The standard further notes that "in designing, implementing, and operating it's QC system, the firm will have to address not only firm personnel but also other auditors and other professionals or organizations that the firm uses in connection with the firm's QC system or the performance of its engagements.". The standard also indicates that "the firm's own QC system must address all the work done on the firm's engagements and in connection with the design, implementation and operation of the firm's QC system itself, regardless of who does it."

   While it is clear how the scope of the Standard applies to certain categories included in the definition of "other participants" such as other accounting firms, other accountants, personnel at shared service centers outside the firm, internal auditors of the client that provide direct assistance to the auditor, specialists engaged by the firm and networks, it is not clear if firms should include other professionals and or organizations that provide advisory services in the design, implementation and operation of the system of quality management as an "other participant" as it is currently defined in the standard. We therefore encourage the Board to provide further clarity on which types of other professionals or organizations that assist the firm with the design, implementation and operation of the firm's system of quality control, should be included in the definition of "other participants".

3. **Provide smaller firms with options that allow for better scaling and cost containment**

   As a practical alternative, we propose amending the rule to provide smaller firms (e.g. triennially inspected firms with less than 100 issuers) with the option to comply with ISQM 1 or SQMS 1 as an acceptable alternative to QC 1000. We believe that this would achieve the same quality objectives and goals without requiring firms to build additional infrastructure. ISQM 1 and SQMS 1 principles-based requirements envision that audit firms will need to adapt the requirements to the varying legal and standard requirements that may apply to an engagement. For 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 a firm or its engagements are subject to them. It does not therefore seem necessary to also require firms to supplement their existing systems with additional requirements.

4. Provide additional time for evaluation and implementation

The proposed rule approximates almost 500 pages. For smaller firms with less resources, the ability to understand and digest the proposal is a significant concern. We remain deeply concerned that smaller firms may not have had adequate opportunity to consider the impact of the proposed standard and the proposed rule. Challenges they may face in practice may therefore have not yet surfaced. Without this additional time or outreach to this group of firms, they may inadvertently be set up for additional inspection and enforcement actions, further increasing their costs and pushing more firms from the marketplace.

We support the PCAOB's efforts to modernize these standards. We remain concerned about the implementation challenges for smaller firms. We would be pleased to discuss our comments with you at your convenience. Please direct any questions to Jackson Johnson, President (jjohnson@jgacpa.com), Joe Lynch, Shareholder and Managing Director (jlynch@jgacpa.com) or Santina Rocca, Managing Director (srocca@jgacpa.com). They may be reached at (702) 848-7084.

Sincerely,

Johnson Global Advisory

Appendix – Copy of Comment Letter to PCAOB February 1, 2023

JOHNSON GLOBAL Accountancy

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.

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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) or Joe Lynch, Managing Director (jlynch@jgacpa.com). They may be reached at (702) 848-7084.

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