



## Insights

Monday, 31 March 2025

### Initial insights from inspections conducted in 2024 at non-PIE audit firms on the implementation of the ISQM 1 standard

In 2024, the Belgian Audit Oversight Board<sup>1</sup> (hereafter 'BAOB') carried out for the first time inspections on the implementation of the International Standard on Quality Management (ISQM) 1 at a selection of non-PIE audit firms. Adopting a pedagogical and awareness-raising approach, the BAOB was able to gain greater insight into the way in which non-PIE audit firms understand and apply the new standard, and how the latter contributes to the risk management of their audit firm and the quality of their audit work.

The inspections focused on the design and implementation of:

- The risk assessment process;
- The 'Human Resources' component;
- The 'Governance and Leadership' component.

The BAOB wishes to share good practices in order to support the sector in their efforts to develop and strengthen their new office organization.<sup>2</sup>

<sup>1</sup> Article 32 of the Law of 7 December 2016 on the organization of the profession and the public supervision of auditors.

<sup>2</sup> For inspiration see the '*ISQM 1 First-Time Implementation Guide*' of the International Auditing and Assurance Standards Board (<https://www.iaasb.org/publications/isqm-1-first-time-implementation-guide>).

## 1. The ISQM 1, a new quality management standard

ISQM 1<sup>3</sup> is aimed at strengthening the quality of assurance activities by introducing a proactive and iterative system of quality management that provides each firm with reasonable assurance that (1) the firm and its personnel comply with the legal, regulatory and normative framework and that (2) engagement reports issued by the firm or engagement partners are appropriate in the circumstances.

In accordance with ISQM 1, all audit firms were required to design and implement such a system of quality management for audit engagements by 15 December 2023<sup>4</sup>, and to evaluate it by 15 December 2024 (ISQM 1.53-54)<sup>5</sup>.

This important change in a firm's organization amounts in fact to replacing a (static) system of quality control (ISQC<sup>6</sup> 1) with a (dynamic) system of quality management (ISQM 1). Whereas the international ISQC 1 standard imposed a quality control procedure, ISQM 1 introduces a dynamic and risk-based approach to quality management.

## 2. First ISQM 1 inspections at non-PIE audit firms in 2024

The BAOB audited the internal organization of 13 non-PIE firms<sup>7</sup> with regard to the design and the implementation of the new system of quality management required by ISQM 1. The main purpose of these inspections was to

- evaluate the design and the implementation of the system of quality management;
- obtain an understanding of the risk assessment process;
- gauge the completeness of the risk assessment (client portfolio, industry specific risks, scope, etc.); and
- assess the adequacy of the responses designed by the firm.

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<sup>3</sup> The International Auditing and Assurance Standards Board adopted its ISQM 1 standard in December 2020. It was transposed into Belgian law by the publication in the Belgian Official Gazette of the standard implementing the international standards for quality management 1 and 2 (ISQM 1 and 2) and of ISA 220 (Revised) in Belgium. The standard is freely available (in French and Dutch only) on the website of the [Institut des réviseurs d'entreprises/Instituut van de Bedrijfsrevisoren](#). According to the standard, a) the design and implementation of a quality management system for audit engagements in accordance with ISQM 1 were to be completed by December 15, 2023 at the latest; b) the application of ISQM 2 to audit engagements was scheduled for periods commencing on or after December 15, 2023; and c) the application of ISA 220 (Revised) to audits of financial statements was scheduled for periods commencing on or after December 15, 2023.

<sup>4</sup> Audit engagement as defined in Article 3, 10°, of the Law of 7 December 2016. All assurance engagements fall under the concept of 'audit engagement' as defined in Article 3, 10°, of that law.

<sup>5</sup> The standard implementing ISQC 1 in Belgium and the ISA 220, Quality control for an audit of financial statements, as provided for by the standard (revised in 2018) implementing the ISAs in Belgium, have been repealed with effect from the date of entry into force of ISQM 1, ISQM 2 and ISA 220 (revised). From that date, any reference to ISQC 1 in a standard is replaced by ISQM 1 and 2. Notwithstanding the above, the standard implementing ISQC 1 in Belgium remains applicable to assignments whose planning phase was completed before the entry into force of ISQM 1 and 2.

<sup>6</sup> International Standards on Quality Control.

<sup>7</sup> Two non-PIE networks with common quality management policies and procedures and 11 non-PIE audit firms.

Two of the thirteen firms had not even started designing and implementing ISQM 1, and were given a compliance deadline to remedy the situation as quickly as possible.

The remaining eleven audit firms had implemented ISQM 1 and received individual letters setting out the findings of the inspection in the form of Key findings, Observations and/or Examples of good practice.<sup>8</sup> This “take no action” approach is perfectly in line with the pedagogical and awareness-raising approach that the BAOB has decided to adopt for the first inspections dedicated to the new internal organization standard.

### 3. Main findings regarding ISQM

The BAOB identified a number of recurring findings, subdivided into three categories, that are detailed below.



**Key findings:** These require the firm to take action to better comply with the ISQM standard and thus improve audit quality. The BAOB will analyze the corrective measures taken during a subsequent inspection.

#### 1. Network requirements or network services

A network firm<sup>9</sup> is, when applicable, subject to ISQM 1.48 – 52.

**Networks may establish requirements regarding the firm’s system of quality management or may make services or resources available that the firm may choose to implement or use in the design, implementation and operation of its system of quality management.**<sup>10</sup> Such requirements or services may be intended to promote the consistent performance of quality engagements across the firms that belong to the network. The extent to which the network will provide the firm with quality objectives, quality risks and responses that are common across the network will depend on the firm’s arrangements with the network.

**The firm may be expected by the network to implement the network requirements. However, the firm may need to adapt or supplement the network requirements such that they are appropriate for the nature and circumstances of the firm and its engagements.** ISQM 1.A179 provides examples of how the network requirements or services may need to be adapted or supplemented.

The BAOB found in a number of cases that the firm had failed to assess the way in which it had to **adapt or supplement the network requirements for appropriate use in the system of quality**

<sup>8</sup> See below.

<sup>9</sup> See ISQM 1.16 (k) and 16 (l) for a definition of “network firm” and “network”.

<sup>10</sup> ISQM 1.A175 provides examples of network services and requirements.

**management** (for example, given the nature and circumstances of the firm, its engagements, laws and regulations, professional standards).

## 2. Specified responses

An essential part of the risk assessment process involves designing and implementing responses. In the design and implementation of responses to quality risks, the firm must take into account the reasons for the assessments of given to those risks.

**ISQM 1.34 lists a number of specified responses to be designed and implemented by a firm, whatever its size or activity.** For example, the firm must obtain at least annually a confirmation of compliance with independence requirements from all its staff members.<sup>11</sup> It must also establish policies or procedures that address circumstances when it is appropriate to communicate with external parties (such as its supervisory authority) about its system of quality management. Another specified response under ISQM 1.34 is the mandatory establishment of policies or procedures for receiving, investigating and resolving complaints.

**The BAOB found in a number of cases that one or several specified responses required by ISQM 1.34 were missing from their system of quality management.** Such was, for example, the case of the establishment of policies or procedures for identifying, evaluating and addressing threats to compliance with the relevant ethical requirements. These policies and procedures are all the more important when the firm is a network member (just think of controls on independence and non-audit services).

## 3. Service providers

**When, for lack of appropriate in-house resources, the firm uses resources from a service provider<sup>12</sup>,** it remains responsible for its own system of quality management.

ISQM 1.A105 lists examples of service providers, such as an individual engaged to perform the firm's monitoring activities or engagement quality reviews, or to provide consultation on technical matters. The definition of a service provider also applies to a commercial IT application used to perform audit engagements. However, it does not include the firm's network, other network firms or other structures or organizations in the network.

In identifying and assessing quality risks, the firm is required to obtain an understanding of the conditions, events, circumstances, actions or inactions that may adversely affect the achievement of the quality objectives, which includes conditions, events, circumstances, actions or inactions relating to service providers.

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<sup>11</sup> ISQM 1.34.(b).

<sup>12</sup> Under ISQM 1.16 (v), a service provider is 'an individual or organization external to the firm that provides a resource that is used in the system of quality management or in the performance of engagements. Service providers exclude the firm's network, other network firms or other structures or organizations in the network'.

With regard to the **exercise of responsibilities in compliance with relevant ethical requirements**, the firm may, for example, decide that the principle of confidentiality applies to service providers when they have access to client information obtained by the firm.

**The BAOB found that a number of firms did not apply the definition of service provider. They had therefore failed to map in their system of quality management the ISQM consequences of using service providers.**



**Observations:** These are **observations** made in relation to initiatives aimed at improving compliance with ISQM 1 and, consequently, audit quality. The BAOB encourages firms to consider implementing these initiatives.

### 1. Ongoing identification and assessment of quality risks

By identifying and assessing quality risks, the firm can proactively take measures to improve the quality of its engagements. **Regular assessment of these quality risks also enables the firm to constantly optimize the quality of its services and to anticipate changes in the nature and circumstances of the firm and its engagements.** The continuous updating of this identification and assessment results in the proactive, dynamic and iterative approach to quality risks sought by the ISQM.

Quality risks change over time, particularly depending on the nature and circumstances of the firm, as well as the way in which the firm is structured and organized.

ISQM 1.A46 lists a number of quality risks that may arise. **The characteristics and management style of leadership** may give rise to people-related quality risks. For example, in the context of governance and leadership, having a smaller firm with a few engagement partners with shared authority may give rise to quality risks such as:

- 'leadership's responsibilities and accountability for quality are not clearly defined and assigned'; or
- 'the actions and behaviors of leadership that do not promote quality are not questioned'.

The same goes for **the complexity and operating characteristics of the firm**. In the context of resources, a firm having recently completed a merger with another firm may identify quality risks such as:

- 'technological resources used by the two merged firms may be incompatible'; or
- 'engagement teams may use intellectual resources developed by a firm prior to the merger, which are no longer consistent with the new methodology being used by the new merged firm'.

The BAOB found in a number of cases that a firm had identified quality risks but that these could be further refined according to specific circumstances, such as the arrival or departure of a partner likely to have repercussions on the system of quality management. The BAOB encourages these firms to further refine their quality risks with a view to proactively managing the quality of the engagements they carry out

## 2. Sources of information enabling the firm to establish quality objectives, identify and assess quality risks, and design and implement responses to these risks.

The way in which quality objectives are established, quality risks are identified and assessed, and responses are designed and implemented varies from one firm to another. The nature and circumstances of the firm, including the way in which it is structured and organized, influence this process.

**In any event, a firm must establish policies or procedures that are designed to identify information that indicates additional quality objectives, or additional or modified quality risks or responses, are needed due to changes in the nature and circumstances of the firm or its engagements.**

ISQM 1.A52 gives a **scalability** example to demonstrate how policies or procedures for identifying information about changes in the nature and circumstances of the firm and its engagements may vary.<sup>13</sup>

**The BAOB found in a number of cases that a firm had not taken external sources of information<sup>14</sup> such as the supervisory authority (the BAOB), the ICCI<sup>15</sup>, the IRE-IBR<sup>16</sup>, etc., into account in its procedures.** It encourages firms to take these external sources of information into account in order to optimize their quality management system and thus improve audit quality.

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<sup>13</sup> In a more complex firm, the firm may need to establish more formal policies or procedures to identify and consider information about changes in the nature and circumstances of the firm or its engagements. This may include, for example, a periodic review of information relating to the nature and circumstances of the firm and its engagements, including ongoing tracking of trends and occurrences in the firm's internal and external environment.

<sup>14</sup> The information the firm uses to establish quality objectives, identify and assess quality risks, and design and implement responses, is taken not only from its own system of quality management (the results of the firm's monitoring process for example), but also from internal and external sources of information.

<sup>15</sup> Centre d'Information du Révisorat d'Entreprises – Informatiecentrum voor het Bedrijfsrevisoraat.

<sup>16</sup> Institut des réviseurs d'entreprises – Instituut voor de Bedrijfsrevisoren.



**Examples of good practice:** These are examples of good practice that the BAOB has noted within the firm and which it encourages the firm to continue to apply.

## 1. Quality management software

A **good working method** that the BAOB observed on several occasions is the **purchase by the firm of a software package with which to document the firm's quality objectives, the quality risks and the responses to these risks.**

**ISQM 1 does not require firms to purchase software** to design their system of quality management. A sole practitioner may also develop an in-house system of quality management that will be proportionate and will meet ISQM 1 requirements.

**A good software package may nonetheless offer advantages** such as better documentation, an integration with other systems and an increased contribution to consistency and uniformity. This is certainly the case for **firms that have a relatively large client base or a number of audit mandates**, and for whom manually updating a dynamic system of quality management is consequently far from easy.

## 2. Identification and assessment of quality risks

Quality risks must always be assessed. However, it is perfectly acceptable but not necessary to do so by means of formal ratings or scores.

**A good working method identified by the BAOB is the approach taken by auditing firms of assigning a likelihood (occurrence) and impact (effect) score to each of their quality risks.**

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