

BY E-MAIL ONLY

International Auditing and Assurance Standards Board

To: Mr. Thomas R. Seidenstein (Chair)

529 Fifth Avenue

New York

10017 USA

Date: September 29, 2020

Subject: Comment on the IAASB proposed revisions to International Standard on Auditing 600 (revised): Special considerations - Audits of Group Financial Statements (including the Work of Component Auditors)

Dear Mr. Seidenstein,

1. The International Forum of Independent Audit Regulators (IFIAR) appreciates the opportunity to comment on the International Auditing and Assurance Standards Board (IAASB) request for input on its Exposure Draft “International Standard on Auditing 600 (revised): Special Considerations - Audits of Group Financial Statements (including the Work of Component Auditors) and Proposed Conforming and Consequential Amendments to Other ISAs” (ED-600). As an international organisation of independent audit oversight regulators that share the goal of serving the public interest and enhancing investor protection, IFIAR is committed to improving audit quality globally through the promotion of high-quality auditing and professional standards, as well as other pronouncements and statements.
2. IFIAR’s objectives are as follows:
  - Sharing knowledge of the audit market environment and practical experience of independent audit regulatory activity, with a focus on inspections of auditors and audit firms.
  - Promoting collaboration and consistency in regulatory activity.
  - Initiating and leading dialogue with other policymakers and organisations that have an interest in audit quality.
  - Forming common and consistent views or positions on matters of importance to its members, while considering the legal mandates and missions of individual members.
3. The comments we provide in this letter reflect the views expressed by many, but not necessarily all of the members of IFIAR. However, the comments are not intended to include, or reflect, all of the views that might be provided by individual members on behalf of their respective organisations.
4. Where we did not comment on certain specific matters, this should not be interpreted as either approval or disapproval by IFIAR.

## Overall comments

5. We support the direction of the proposed standard to clarify the linkages with other standards and address special considerations in an audit of group financial statements, including highlighting the requirements when a component auditor (CA) is involved. However, as noted by our comments in this letter, we believe there are areas where: (1) the linkages to other standards could be further emphasized, (2) some requirements could be strengthened, and (3) application material could be added to further improve the standard thereby driving consistent application with the ultimate goal of enhancing audit quality.
6. We strongly recommend that the IAASB aim to finalize the amended standard as expeditiously as possible and no later than June 2021 (rather than September 2021). We believe the earliest effective date of ED-600 could be for audits of companies with year-ends beginning on or after December 15, 2022; which is aligned with the anticipated effective dates for the revised quality management standards, ISA 220 *Quality control for an audit of financial statements*, International Standards on Quality Management (ISQM) 1 and ISQM 2.

## Scope and applicability

7. While an auditor view of the entities and business units comprising the group for the purpose of planning and performing the group audit may provide more flexibility and potentially assist with the scalability of the standard, the level of complexity in practice for auditors may increase the risk of inappropriate application. There may be an increased risk of inappropriate scoping to achieve efficiencies in the audit at the cost of quality. For example, there is a risk that the group auditor may group entities and treat them as a homogeneous population when it is not appropriate and/or inconsistent with the facts and circumstances of the entities. We recommend the IAASB consider a requirement for the group engagement team (GET) to document its rationale when the auditor's view of the components differs from management's and the consequential impact of this on the risk assessment, testing of internal controls and substantive testing.

## Risk assessment

8. We support the direction of the standard and the stronger linkage to the requirements of ISA 315 *Identifying and assessing risks of material misstatement* and ISA 330 *The auditor's responses to assessed risks*. The IAASB could further enhance ED-600 in a few key areas:
  - The application material in A 97 proposes three approaches to assigning audit procedures when the GET uses a CA. There is limited guidance to determine when these approaches would apply. Further guidance could better support the GET's decisions when assigning responsibility for the design of further audit procedures to the CA, including, for example, providing better linkage between A 97 and A 98 to A 101.
  - As part of the assessment of risks at the group financial statement level, the GET should, where CAs are involved, request the CA provide input to the relevant risk assessments at the component level which are relevant for the group audit in order to benefit from the CA's knowledge of the component and its environment.

## Materiality and aggregation risk

9. We support the direction of the new component performance materiality definition in paragraph 9 (e) of ED-600, which is to set component performance materiality to an appropriately low level to reduce aggregation risk. Additional qualitative considerations are necessary to assist auditors in determining component performance materiality while considering aggregation risk. Examples of such considerations include but should not be limited to the, potential effect on loan provisions, debt covenants, contractual arrangements, implication for fraud/illegal acts, existence of statutory or regulatory reporting requirements, etc.
10. Paragraph A 73 indicates that a different component performance materiality may be established for each component where audit procedures are performed. This should be developed further as a requirement which should clearly state that consideration should be given to the need for a separate component materiality to be determined for each component based on the specific characteristics and facts (A 75).

## Consideration of fraud in the audit of group financial statements

11. Further guidance supplementing paragraphs 34 and 35 should be included given the importance of the consolidation process to the group financial statements. Frauds can be perpetrated via consolidation and other adjustments. Therefore, we recommend including additional references to the risks of material misstatement due to fraud, including increased susceptibility to fraud in relation to the consolidation process.
12. In addition, the guidance in A 80 which states that the auditor may consider whether the risk of material misstatement due to fraud is higher for particular components should instead be a requirement to consider whether and how identification and assessment of fraud risks may vary by component.

## Communication

13. To reinforce the two-way communication between the GET and CA and the GET's direction and supervision of CAs, we encourage the IAASB to add the following items to the requirements listed in paragraph 44:
  - A 116 states that a group engagement partner's (GEP) evaluation may consider whether misstatements communicated by CAs indicate a systematic issue. This should be a requirement for the GET to request the CA to communicate identified and corrected misstatements in addition to uncorrected misstatements. This may assist the GET in performing the 'stand-back' requirement, including understanding whether there are pervasive issues in the group, which could indicate similar uncorrected misstatements in other components or controls that are not operating effectively that could impact initial risk assessments.
  - There is no explicit requirement for the CA to communicate matters and/or accounts balances where the CA made significant judgments that are different from those communicated by the GET to the CA, including the nature of those judgements made by the CA. This should be included as a required communication by the CA to the GET as it may assist the GET in its application of ISA 701 *Communicating key audit matters in the independent auditor's report* at the group level.

## **Component auditor oversight**

14. There is limited guidance on when a group auditor is expected to visit CAs or when the GET should review the CA's documentation. It is unclear how the risk-based approach used to determine the work efforts of the CA could translate into the actual procedures expected to be performed by the GET and/or CA. ED-600 proposes that the higher the auditor's assessment of risk, the more persuasive audit evidence needs to be obtained and more involvement of the GET would be expected. The requirements in paragraph 32 should include additional application material on actions the GET can take as the risk associated with a component increases, either due to significance or risks assessed at the higher end of the risk spectrum, combined with the knowledge, skill and ability of the CA.
15. The proposed ED-600 leaves too much flexibility for the GET to conclude that it is not necessary to visit or review the working papers of the CA where the CA is part of the same network of firms. Paragraph 45 (b) states that the GET is required to "determine whether, and the extent to which, it is necessary to review parts of the CA's audit documentation". We recommend that the requirements be strengthened by moving the application material in A 113 into the requirements section. Also, further application guidance is necessary to understand to what extent the firm's policies or procedures impacts the nature, timing, and extent of the GET's review of the CAs documentation.

## **Restrictions on access to information and people**

16. The proposed ED-600 includes details on how to address and/or overcome restrictions on the GET's access to information and/or people for the audit. Specifically, paragraph A 30 refers to the GET's communication with the GET's firm who in turn may communicate with regulators, listing authorities or others, about the restrictions and may encourage group management to communicate with regulators. It is not clear what the objective or purpose of such communication is or how it helps overcome the concerns arising from the access to information and/or people. While we support the direction of the proposed revisions, additional guidance is needed to understand and demonstrate how aspects of access restrictions could be overcome.

## **Documentation requirements**

17. The requirements of paragraphs 57, and the related application material in A 126 to A 130 of ED-600, include clear linkages to ISA 230. These demonstrate what is expected by the GET. However, we recommend including additional requirements with the appropriate application material related to the level of detail expected to support the GET's review of the CA working papers. The GET should be required to demonstrate the extent of oversight, and how the GET reached its conclusions regarding the sufficiency and appropriateness of the nature and extent of procedures performed by CAs.

## Quality management standards

18. Additional application material is necessary to understand the interrelationship between ED-600 and ISQM 1/ISQM 2 with respect to the responsibilities of the GET and reliance on the firm's system of internal controls. Specifically,
- A 20 of ED-600 discusses common policies and procedures established by the firm that are common and may support the GEP by facilitating communication between the GET and CAs. We suggest clarifying the link between the policies and procedures of the firm or common network requirements or network service and how the GET may use this information for communications. It is also unclear how the automated tools or techniques discussed in A 45 are different from those discussed in A 44.
  - There should be stronger linkage to ISQM 1 in A 42 to A 44 regarding the competence and capabilities of the CAs.
  - A 39 of ED-600 should be enhanced to emphasize the GET's and CA's responsibility over compliance with the relevant ethical requirements, including those related to independence. Specifically, potential threats to compliance with independence requirements may arise in group audits with multiple components, including with respect to the allocation of fees and other remuneration arrangements. Further, personal financial investments in, or other financial arrangements made by component auditors with, the consolidated entity are clear independence issues and should be prohibited. We recognize that independence and ethical standards are handled by separate standard setting bodies, but it is vitally important that those charged with governance and the users of the audit report be aware of the existence of any such situation. We recommend additional guidance including a clear linkage to paragraph 17 of ISA 260, *Communication with those charged with governance*, to support the independence requirements.

## Implementation guidance

19. The IAASB should consider how to address instances that may arise in the first year of implementation where GETs and the firm rely on policies and procedures at a network firm that have been implemented but not yet evaluated in accordance with the requirements of new ISQM1. We recommend including guidance and/or application material in conjunction with ISQM 1, including any responses/policies and procedures that may be relevant that the GET relied on.

Should you wish to discuss any of our comments, please do not hesitate to contact me or Martijn Duffels, Chair of the IFIAR Standards Coordination Working Group.

Yours Faithfully,



Franck Schneider  
IFIAR Chair

Cc: Duane M. DesParte, IFIAR Vice Chair,  
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