Dear Sir:


We are pleased to have the opportunity to comment on the above Exposure Draft issued by the International Auditing and Assurance Standards Board (IAASB). We support the exposure draft and its aim to improve the quality of audits of group financial statements. Our responses to the questions posed in the explanatory memorandum and our comments on the proposals are set out below.

Is the approach to the work of other auditors practical, having regard to elimination of the divided responsibility option?

We support the elimination of the divided responsibility option and resulting requirement for the group auditor to take responsibility for the audit opinion of the group financial statements. We accept that with the elimination of the divided responsibility option, the group auditor’s involvement in the work of other auditors will increase. We also believe that such increased involvement should be built on the overarching concepts in ISQC 1 and ISA 220 that enable auditors to rely, when appropriate, on firm systems and on the qualifications and competencies of other auditors in determining the extent of work to be carried out. While we agree with the general direction of the proposed ISA, we have concerns with the following areas:

(a) Extent of Group Auditor Involvement in the Risk Assessment of a Significant Component

For significant components, paragraph 61 requires the group auditor to be involved in the other auditor’s risk assessment to identify significant risks of material misstatement of the group financial statements. While we agree with this principle, we disagree with the grey lettered requirement in
paragraph 62(a) that interprets “involvement” to include discussion by the group auditor or related auditor with component management regarding the component’s business activities that are significant to the group. We believe that this type of involvement on the part of the group auditor or related auditor is not necessary in all audits involving significant components audited by another auditor. Further, we are concerned that this requirement may be unrealistic for audits involving components that are joint ventures or associated companies since it may not be feasible for the group auditor or related auditor to participate in such discussions. We believe that the extent to which the group auditor or related auditor is involved in the risk assessment of a significant component should be left up to the group auditor’s judgment after considering the professional qualifications, independence and professional competence of the other auditor as well as the quality control systems of his or her firm as discussed in paragraph 29 of the proposed ISA. The group auditor should determine, in his or her professional judgment, that effective risk assessment procedures have been performed.

We therefore recommend that 62(a) be modified to clarify that group auditor or related auditor involvement in discussions with component management will depend on the group auditor’s assessment of the professional qualifications, independence and professional competence of the other auditor who is auditing that component.

(b) Group Auditor’s Evaluation of the Other Auditor’s Work

Paragraph 80 of the proposed standard requires the group auditor to review relevant parts of the other auditor’s “audit documentation” when the other auditor performs work on the financial information of a significant component. When the other auditor is an unrelated auditor, the standard allows for a related auditor to perform the review on behalf of the group auditor, in which case the group auditor reviews the related auditor’s review memorandum, including the conclusions reached on the adequacy of the work of the unrelated auditor for the group auditor’s purposes. When the other auditor is a related auditor, we interpret the standard to require the group auditor to review relevant parts of the other auditor’s “audit documentation” (defined as “workpapers” by ISA 230), and that it is not sufficient for the group auditor to review a memorandum prepared by the related auditor. Given the overarching concepts in ISQC 1 and ISA 220, we question why it is necessary for the group auditor to review the working papers of a related auditor when the related auditor performed the work on a significant component and is part of a network operating under common monitoring policies and procedures. We believe that in these circumstances the group auditor should be able to rely on the firm’s systems and on the results of the monitoring process implemented within the network. This should enable the group auditor to carry out the evaluation procedures required by paragraph 29 and conclude that a review of the related auditor’s working papers is not necessary.
We therefore recommend that paragraphs 80 to 83 of the proposed standard be modified to enable the group auditor to review the documentation (as opposed to relevant parts of the “audit documentation”) of a related auditor who is part of a network operating under common monitoring policies and procedures. We also recommend that the proposed standard clarify that such “documentation” may be in the form of a memorandum of the work performed and conclusions reached on a significant component and that it differs from “audit documentation”.

(c) Consideration of Professional Competence of Related and Unrelated Auditors

We support the requirement for the group auditor to consider the professional qualifications, independence, and professional competence of the other auditors, and the quality control systems of their firms. We also support the notion that such consideration will affect the nature, timing and extent of the group auditor’s involvement in the other auditor’s work. However, we have some concerns with the required procedures and guidance that the revised standard proposes for the consideration of both related auditors and unrelated auditors.

Related Auditor

Paragraph 31 states that the group auditor can ordinarily rely on the quality control policies and procedures of a related auditor’s firm regarding the related auditor’s professional qualifications, independence and professional competence. However, in the case of significant components, when the group auditor does not have personal knowledge of the related auditor’s professional competence, paragraph 34 requires the group auditor to work with the related auditor’s firm to determine whether the related auditor has the necessary professional competence.

We question the need for this additional requirement as it seems to be contrary to the principles underlying ISA 220 and ISQC 1. ISQC 1.36 requires a firm to establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the capabilities and competence to perform its engagements. ISQC 1.42 states that the firm should assign responsibility for each engagement to an engagement partner who has the appropriate capabilities, competence, authority and time to perform the role. In addition, if a particular firm in the network has deficiencies with respect to assignment of engagement partners, the network firm’s monitoring program as required by ISQC 1.74 to 86 would identify such deficiencies which would then be communicated to firms within the network as per ISQC 1.87. Paragraph 32 of the proposed ISA requires the group auditor (engagement partner or team member) to consider the results of the communications made per ISQC 1.87 and whether any deficiencies have been appropriately addressed.

Given these requirements, we question why the group auditor is not able to rely on the related auditor’s firm to ensure that the partner assigned to the engagement meets the requirements in ISQC 1.42.
We recommend that paragraph 34 of the proposed standard be deleted given that its objectives are covered by other paragraphs in the ISAs and ISQC 1 as discussed above.

**Unrelated Auditor**

Paragraphs 36 and 37 of the proposed standard discuss the group auditor’s procedures relating to consideration of unrelated auditors. We agree that the group auditor’s required work effort regarding consideration of the other auditor will be more onerous when the other auditor is an unrelated auditor. We generally support the nature of the procedures required by the proposed standard; however, we do have some recommendations relating to the confirmations that are requested by the group auditor and the group auditor’s reliance on external quality control review reports. These are discussed below.

*Group Auditor’s Confirmation*

Paragraph 36 of the proposed ISA requires the group auditor to confirm whether there are any issues noted in recent monitoring reports that are likely to significantly affect the work that the unrelated auditor will perform on the financial information of the component.

It is not clear whether the intention of paragraph 36 is to have the unrelated auditor report all relevant findings included in monitoring reports or only those findings that have not been addressed by the unrelated auditor and/or his or her firm. ISQC 1.83 requires firms to evaluate deficiencies and take appropriate action to address issues noted. Accordingly, it is possible that such issues noted in recent monitoring reports may have been mitigated and therefore no longer relevant to the group.

We therefore recommend that IAASB revise paragraph 36 to clarify that the group auditor is required to seek confirmation of matters noted in recent monitoring reports that are likely to significantly affect the work that the unrelated auditor will perform on the financial information of the component **that have not been appropriately addressed by the unrelated auditor**. We believe that the group auditor does not need to seek confirmation of matters that have been appropriately addressed by the unrelated auditor given that these matters are no longer likely to affect the work that the unrelated auditor will perform on the financial information of the component.

Paragraph 37 requires the group auditor to obtain a copy of any report of the unrelated auditor’s latest review that is published by the body responsible for conducting external quality control reviews, and is publicly available.

We find the objective of paragraph 37 and the external reports it is referring to unclear. The reference to unrelated auditor is ambiguous as it is not clear whether the requirement to obtain a
copy of the unrelated auditor’s latest review is intended to apply to the firm or the engagement partner. We also question whether it is reasonable to require the group auditor to obtain copies of external reports given that he or she may not be familiar with the quality control review process followed by the relevant bodies in the unrelated auditor’s jurisdiction. To address this, we recommend that the proposed standard require the group auditor to ask the unrelated auditor to provide copies of review reports on the firm that were published by the body (bodies) responsible for conducting external quality control reviews. Paragraph 37 should also discuss the need for the group auditor to follow up with the unrelated auditor on any matters that are reported and that may be relevant to the work that the unrelated auditor will perform on the financial information of the component. Lastly, we also recommend that paragraph 37 clarify that the review reports being referred to are those that relate to the independent external inspection programs mentioned in ISQC 1.79, if this indeed is the IAASB’s intention.

**Are the revised standards and guidance on accepting or continuing an engagement to audit group financial statements appropriate?**

We agree with the principle in paragraph 7 of the proposed ISA that requires engagement acceptance to be based on the group auditor’s assessment of obtaining sufficient appropriate audit evidence on which to base the audit opinion on the group financial statements. We also agree with the criteria for identifying significant components in paragraphs 15 and 16 of the revised standard, except for the inclusion of a specific percentage as a benchmark in paragraph 16 (“20%”). While we recognize that this percentage is intended to guide auditors and that paragraph 16 specifically mentions that a lower percentage may be more appropriate, we are concerned that auditors may feel obliged to adhere to the percentage included in a standard in an effort to be consistent with the ISAs. We also have the same observation regarding the use of 5% in paragraph 54 as a possible benchmark to identify components that in aggregate are not significant.

We therefore recommend that paragraphs 16 and 54 be modified to remove reference to specific percentages. Instead, we recommend that these paragraphs state that the group auditor may determine a range of possible percentages to be applied to a chosen benchmark based on the nature and circumstances of the group.

**Do the revised standards and guidance on access to information, given various laws of jurisdictions, give rise to any unnecessary foreseeable difficulty?**

Paragraph 18 prevents a group auditor from accepting an engagement when his or her access to component information, those charged with governance or other auditors will be restricted and the group auditor’s inability to obtain sufficient appropriate audit evidence is material and pervasive to the group financial statements. We question the appropriateness of this principle when it relates to the audit of significant components accounted for by the equity method. Paragraph 21 suggests that for significant components a restriction in access to component information, those charged with
governance or component management will result in a lack of sufficient appropriate audit evidence. We disagree with this conclusion and believe that in some circumstances it should be possible for the group auditor to conclude that the audited financial statements of a significant component accounted for by the equity method constitute sufficient appropriate audit evidence. This should be the case when the auditor is able to make a determination regarding the other auditor’s professional qualifications, independence, and professional competence based on personal experience or the experience of a related auditor.

We recommend that paragraphs 18 to 23 provide more flexibility as to what may constitute sufficient appropriate audit evidence for a significant component accounted for by the equity method when the group auditor faces restricted access to information for that component. Such flexibility can be provided by adding guidance indicating that in some circumstances it may be possible for the group auditor to conclude that the audited financial statements of the component constitute sufficient appropriate audit evidence when the group auditor is able to rely on information already obtained about the professional qualifications, independence, and professional competence of the component’s independent auditor, and of the quality control systems of that auditor’s firm.

Is the proposal to move the guidance originally contained in the proposed IAPS to the proposed ISA appropriate?

We support the IAASB’s decision to move the guidance originally contained in the proposed IAPS to the proposed ISA.

Other Substantive Points

Definition of Group Auditor

We have concerns with the definition of group auditor in the proposed revised ISA 600. The proposed ISA states the following:

- Group auditor means the auditor who signs the auditor’s report on the group financial statements.
- The term “auditor” is used to describe either the engagement partner or the audit firm.
- Where it applies to the engagement partner, it describes the obligations or responsibilities of the engagement partner. Such obligations or responsibilities may be fulfilled by either the engagement partner or a member of the audit team.
Where it is expressly intended that the obligation or responsibility be fulfilled by the engagement partner, the term “engagement partner” rather than “auditor” is used.

This last bullet means that when the term “group auditor” as opposed to “engagement partner” is used in the proposed ISA the relevant obligation or responsibility may be fulfilled by either the engagement partner, a member of the audit team or the audit firm.

Firstly, we question why the term “audit team” is used when ISA 220 uses the term “engagement team”. More importantly, we are concerned that such a broad definition of “auditor” creates ambiguity and will lead to inconsistent application.

For example, paragraph 77 of the proposed ISA requires the group auditor to evaluate the adequacy of the work of another auditor for the group auditor’s purposes. If the definition of “auditor” for the purposes of applying this requirement is interpreted to mean the audit firm as opposed to the engagement partner or a member of the engagement team, then it is possible to conclude that a group auditor would not be required to evaluate the adequacy of the work of a partner from another office within the same firm operating in a specific country. We do not believe that this is an appropriate interpretation. On the other hand, if the definition of “auditor” is interpreted to mean only the “engagement partner”, then we believe that it would be very difficult for one person alone to meet the requirements of this paragraph.

To avoid such wide ranging interpretations, we recommend that IAASB consider revising the definition of group auditor so that it more narrowly focuses on the responsibilities of the engagement partner and the engagement team. We also recommend that the proposed ISA use the term “engagement team” instead of “audit team” to be consistent with ISA 220. Lastly, there may also be merit to narrowing the definition of engagement team to members under the direct supervision of the engagement partner. This can be achieved by defining the term “auditor” for the purposes of this ISA as follows:

“The term "auditor" is used to describe the obligations and responsibilities of the engagement partner. Such obligations or responsibilities may be fulfilled by either the engagement partner or another member of the engagement team under the direct supervision of the engagement partner. Where it is expressly intended that the obligation or responsibility be fulfilled by the engagement partner, the term "engagement partner" rather than "auditor" is used.”

Materiality

Paragraph 47 of the proposed standard states that to allow for aggregation of identified misstatements and possible undetected misstatements, the component materiality level(s) are lower
than group materiality level(s). Paragraph 49 also states that the auditor responsible for performing
the work on a component ordinarily establishes one or more levels of tolerable error lower than the
materiality levels referred to in paragraph 47.

While we agree with the basic principle set out in paragraph 47, we are concerned that the terms
“group materiality level”, “component materiality level” and “tolerable error” are not clear and may
be interpreted as requiring auditors to set progressively lower materiality levels for components as
they descend down the organizational hierarchy. We find this concept counter intuitive as this
would have the effect of increasing the work effort as the significance of the component to the
group financial statements decreases.

To address the above concerns, we recommend that IAASB revise paragraphs 45 to 49 of the
proposed ISA to clarify:

- The concept of “component materiality levels” refers to levels of precision at which work at the
  assertion level may be performed to allow for aggregation of identified misstatements and
  possible undetected misstatements.

- Such precision levels are often set by reference to materiality required for local statutory or
  other reporting purposes in the jurisdictions in which the respective components operate. The
  proposed standard discusses such local statutory or regulatory audit requirements in paragraphs
  57 and 58; however, it does not link this discussion to the discussion of materiality in
  paragraphs 45 through 49.

- The auditor may set different levels of precision for different assertions or components in order
  to address identified risks or when such levels are required in order to obtain sufficient
  appropriate audit evidence to support the group opinion.

- The meaning of tolerable error and its relationship to the above concepts.

- The intention of the standard is not to set progressively lower materiality levels for components
  as they descend further down the organizational hierarchy.

**Communications with An Other Auditor**

The standard discusses, in some detail, the communication requirements of the group auditor
including the confirmations the group auditor is required to obtain from the other auditors. The
standard does not however, explicitly discuss the other auditors’ communication responsibilities and
the need to respond, in a timely manner, to the confirmation requests of the group auditor.
Guidance and standards in the proposed ISA relating to the other auditor’s responsibilities will help ensure other auditors respond appropriately to requests from group auditors.

We therefore recommend that the ISA include a section establishing standards and explanatory guidance relating to the other auditor’s responsibilities. Such standards and guidance should clarify that the other auditor has responsibilities which include:

- Responding on a timely basis to confirmation requests from the group auditor.
- Bringing to the group auditor’s attention on a timely basis any matters that may be of significance to the group financial statements and the group auditor’s opinion thereon.

Other Comments

Paragraph 17

This paragraph appears to relate more to the auditor’s response to assessed risks than to engagement acceptance and continuance. On this basis we recommend that this paragraph be relocated closer to paragraph 55.

Paragraph 28

The group auditor would ordinarily be expected to consider the standing of any firm which whom the other auditors are affiliated. We recommend that guidance in this regard be included as an additional example in paragraph 28.

Paragraph 36

The “person assigned operational responsibility for the firm’s quality control system” referred to in this paragraph is likely referring to the discussion in ISQC1.76 which states that “the firm entrusts responsibility for the monitoring process to a partner or partners or other persons with sufficient and appropriate experience and authority in the firm to assume that responsibility”. We recommend that the linkage between these two paragraphs be made clearer by either defining the role or by including a reference to ISQC 1 paragraph 76 within the proposed revised ISA 600.

Paragraphs 54 & 55

We believe that the flow of the ISA would be improved if the order of paragraphs 54 and 55 were reversed so that “Components that are Not Significant in the Aggregate” follows “Components that are Significant in the Aggregate”. 
Paragraph 62 (c)
We believe the reference to “related auditor” in the second sentence should actually be to “unrelated auditor” in order appropriately capture the requirements of this paragraph.

Paragraph 78, third bullet
The guidance in the third bullet in paragraph 78 follows from paragraphs 27 and 29 of the proposed standard. However, paragraph 78 is not consistent with these paragraphs. Rather than requiring the group auditor to “consider” the qualifications of the other auditor, paragraph 78 requires the group auditor to “evaluate” such qualifications. Accordingly, we recommend the following change to paragraph 78 to make it consistent with the requirements of paragraphs 27 and 29:

“The group auditor’s evaluation of the professional qualifications, independence, and professional competence of the other auditor….”

Paragraph 85
In accordance with this paragraph, if the group auditor determines that the work performed by an other auditor does not represent sufficient appropriate audit evidence, the group auditor may request the other auditor to perform additional procedures. The paragraph states that if this is not feasible, the group auditor performs further procedures. We believe that it is important for the proposed standard to acknowledge that the procedures performed by the group auditor may differ depending on whether the other auditor is a related or unrelated auditor. We also believe when the other auditor is an unrelated auditor, another viable option is for the group auditor to request a related auditor to perform additional procedures on behalf of the group auditor.

We therefore recommend that the paragraph be expanded to provide guidance on how the group auditor’s procedures may differ depending on whether the other auditor is a related or unrelated auditor. Further, we recommend that the paragraph be modified as follows to allow for a related auditor to perform the additional procedures on behalf of the group auditor when the other auditor is an unrelated auditor:

“If this is not feasible, the group auditor, or a related auditor on behalf of the group auditor, performs additional procedures.”

Paragraph 87
Similar to our comments regarding paragraph 85 above, we believe that the additional audit procedures referred to in this paragraph may be performed by a related auditor on behalf of the group auditor.
Paragraph 103(g)

We believe it is important for the group auditor to be aware of both uncorrected and corrected misstatements identified by the component auditor. We therefore recommend that paragraph 103 (g) be expanded to include reference to corrected misstatements in addition to uncorrected misstatements.

Yours truly

Sylvia Smith
International Desk on Auditing Standards