ED-600 Question 8 – Will the Risk-Based Approach Result in an Appropriate Assessment of the RoMM of the GFS and the Design and Performance of Appropriate Responses to Those Assessed Risks

Question 8:

Will the risk-based approach result in an appropriate assessment of the risks of material misstatement of the group financial statements and the design and performance of appropriate responses to those assessed risks?

In particular, the IAASB is interested in views about:

(a) Whether the respective responsibilities of the group engagement team and component auditors are clear and appropriate?

(b) Whether the interactions between the group engagement team and component auditors throughout the different phases of the group audit are clear and appropriate, including sufficient involvement of the group engagement partner and group engagement team?

(c) What practical challenges may arise in implementing the risk-based approach?

Note: for the purposes of the NVivo analysis, responses on this question were separated between three parts: question Q8, Q8(a)” and “Q8(b)”. Question 8(c) will not be discussed at the December 2020 IAASB meeting.

Q8 - Agree

1. Monitoring Group

BCBS

Risk-based approach

The Committee supports the development of the risk-based approach for the audits of group financial statements. Against the backdrop of the complexity and diversity of banking groups, we believe a risk-based approach of identifying and addressing the risks of material misstatements in the group financial statements is an effective way to foster audit quality for banking groups. We consider the risk-based approach a considerable improvement on the extant approach set out in ISA 600.

The Committee strongly supports the development of the risk-based approach for the audits of group financial statements. Against the backdrop of the complexity and diverse activities of many banking groups, we believe the risk-based approach of identifying risks of material misstatements and minimising them through focusing the audit resources is an effective way to foster quality for the audit of banking groups.

IAIS

The adoption of a risk based approach and increased linkages with other standards. The audit of group financial statements is an audit as any other, and so it is right to emphasise that the other standards are applicable (including ISA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment). Compared to the current standard, a risk-based approach
should lead to a better assessment of the potential risks of material misstatement, and selection of procedures to address these risks.

3. Regulators and Audit Oversight Authorities

CSA

Overall, we support the proposals

MAOB

The Audit Oversight Board, Malaysia (AOB) supports the efforts of the International Auditing and Assurance Standards Board (IAASB) in proposing an enhanced risk-based approach which concentrates on identifying, assessing and responding to risk of material misstatements when performing audit of group financial statements.

UKFRC

We strongly support the new approach and believe that it has the potential to drive significant improvements in the assessment of the risks of material misstatement of the group financial statements and the design and performance of responses to those assessed risks. The approach in extant ISA 600 is a ‘bottom-up’ approach and counterintuitive to the principles of ISA 315 and ISA 330. As a result, the responses to risks of material misstatement at the group financial statement level may not be appropriate in the circumstances (e.g. audit resources are targeted on testing transactions and account balances of the component’s financial information without any particular focus on a testing strategy that responds group risk).

In our outreach activity, stakeholders supported the revisions in this area, noting that the change to a risk-based approach will lead to a greater understanding of the overall risks at the group financial statement level. We believe these changes will: reinforce the risk-based approach that is foundational to an ISA audit; better support the auditor’s conclusion that sufficient appropriate audit evidence has been obtained; offer a principles-based and flexible approach to address current and evolving group structures in a reasonably consistent manner; and address stakeholder concerns about poor understanding and application of concepts like component materiality (discussed further in our response to Question 10), what is required under the ISAs to “audit or review a component” and challenges regarding the work effort for non-significant components.

4. National Auditing Standard Setters

AICPA

For those questions that we have not provided a response, we have no further observations or comments.

HKICPA

We agree that the proposed risk-based approach in ED-600 is suited to addressing a wide range of group audit engagements and enhancing assessment and identification of the risks of material misstatements, thereby driving more appropriate responses.
5. Accounting Firms

CG
We welcome the risk-based approach and consider that this will result in an appropriate assessment of the risks of material misstatement of the group financial statements as well as appropriate responses to the assessed risks. The greater alignment with the requirements of ISA 315 (Revised 2019) and ISA 330 is important.

PKF
The shift to a risk-based approach is certainly welcomed and aligns well with the revisions made to ISA 315 (Revised 2019) and ISA 540 (Revised).

RSM
We consider that the risk-based approach in ED-600 will result in more focussed risk assessments, and therefore responses, which, in turn, will improve audit quality.

6. Public Sector Organizations

AGO
We agree the risk-based approach is appropriate.

AGSA
The risk based approach will assist the group engagement team to direct the focus of the group audit to the risky areas in order for the component auditors to appropriately and sufficiently respond and reduce the group audit risk to an acceptably low level.

PAS
Yes, the risk-based approach should result in an appropriate assessment of the risks of material misstatement of the group financial statements and the design and performance of appropriate responses to those assessed risks.

7. Member Bodies and Other Professional Organizations

CPAI
We welcome many of the proposals in this consultation. In particular, we welcome the enhanced approach to the use of professional scepticism throughout the group audit and the focus placed on identifying and assessing the risks of material misstatement of the group financial statements.

ICAS
If properly undertaken, the risk-based approach should result in an appropriate assessment of the risks of material misstatement of the group financial statements and the design and performance of appropriate responses to those assessed risks.

In particular, we welcome the focus placed on the auditor’s judgement in allowing flexibility as to the most appropriate audit strategy to ensure an effective and efficient audit of group financial statements. We also
welcome the inclusion of a requirement on “Leadership responsibilities” for managing and achieving quality on a group audit, early on in the proposed standard.

SRO AAS

The risk-based approach is critical to group audits, even if there are serious doubts about the need to scale up during the trial testing process (i.e. applying this approach to larger groups with a more complex organisational structure).

Q8 – Agree with comments

1. Monitoring Group

IFIAR

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.

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:

IOSCO

Separately, we note that the Board recently completed ISA 315 (Revised 2019), Identifying and Assessing the Risks of Material Misstatement. While we generally agree with the Board that the requirements and application materials in the Paper are consistent with the revisions in ISA 315 (Revised 2019), we are concerned that the removal of the concept of “significant component” might have unintended consequences, including challenges for auditors to consistently apply the standard, potentially reducing the work performed by auditors thus potentially reducing audit quality in a group audit.

To compound our concern, we observe that there is no guidance for the minimum work effort required to be performed on components. We believe the retention of the concept of “significant component” with enhanced procedures around the risk of material misstatement, enhanced communication requirements from component auditor to group auditor (as well as component to component communication, where appropriate) would be a more effective approach in driving auditors to perform sufficient audit procedures.

We encourage the Board to consider updating a closely related standard, ISA 330, the Auditor’s Responses to Assessed Risks. The Board should consider updating this standard more holistically when it develops its Work Plan for 2022 – 2023 so that ISA 330 can better reflect the risk-based approach other recently updated ISAs have incorporated.

We agree with paragraph 31 that states:

“In applying ISA 315 (Revised 2019), Identifying and Assessing the Risks of Material Misstatement, based on the understanding obtained in paragraph 24, the group engagement team shall take responsibility for the identification and the assessment of the risks of material misstatement of the group financial statements.”

We agree that it is appropriate for the group engagement team to take responsibility for the risk assessment with respect to the group financial statements taken as a whole. However, it is still unclear how the component auditor’s assessment of risk at the component level is expected to affect the group engagement
team’s assessment (or vice versa). For example, should the group auditor be providing its group level risk assessment to the component auditor to assist in determining the extent of risk and procedures to be performed at the component level (or is it vice versa, or continuous, etc.)?

3. Regulators and Audit Oversight Authorities

**CEAOB**

Risk-based approach

We are supportive of the introduction of the risk-based approach in auditing the financial statements of a group and greater alignment with the requirements in ISA 315. The risk-based approach in ED 600 requires the group engagement team to determine the significant classes of transactions, account balances and disclosures in the group financial statements and to identify and assess the related risks of material misstatements of the group financial statements.

However, we are concerned that the group engagement team might perform a centralised risk assessment without giving adequate consideration to the involvement of component auditors (e.g. without choosing to assign work to them, as described in paragraph 25). Paragraph A79 and Appendix 1 provide guidance on the involvement of component auditors. However, there is no requirement in ED 600 to make use of the experience of component auditors and to benefit from their knowledge about the economic, legal and social framework the components operate in. If component auditors are involved, we suggest requiring the group engagement team to request their input as part of the risk assessment process and where deemed necessary in the design of further audit procedures, including where the group engagement team decides to perform these tasks centrally.

More generally, we are of the view that the introduction of the new risk-based approach proposed in ED 600 will require a substantial change in mind-set for auditors and the IAASB should consider what additional guidance can be provided to assist with this shift and to help auditors and audit firms to embrace the new mind-set. For example, the standard refers to the risk-based approach for determining the work efforts required to assess the component auditors’ work, but it does not provide clear provisions on how that risk-based approach impacts the actual procedures to be performed by the group engagement team.

**CPAB**

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 A 97 proposes three approaches to assigning further audit procedures when the group engagement team uses a component auditor. There is limited guidance to determine when these approaches would apply. Additional guidance could better support the group engagement team’s decisions when assigning responsibility for the design of further audit procedures to the component auditor 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 group engagement team should, where a component auditor is involved, request the component auditor provide input to the relevant risk assessments at the component level for the group audit in order to benefit from their knowledge of the component and its environment.
IAASA

Risk-based approach

We are supportive of the introduction of the risk-based approach in auditing the financial statements of a group and greater alignment with the requirements in ISA 315. The risk-based approach in ED 600 requires the group engagement team to determine the significant classes of transactions, account balances and disclosures in the group financial statements and to identify and assess the related risks of material misstatements of the group financial statements.

However, we are concerned that the group engagement team might perform a centralised risk assessment without giving adequate consideration to the involvement of component auditors (e.g. without choosing to assign work to them, as described in paragraph 25). Paragraph A79 and Appendix 1 provide guidance on the involvement of component auditors. However, there is no requirement in ED 600 to make use of the experience of component auditors and to benefit from their knowledge about the economic, legal and social framework in which the components operate. If component auditors are involved, we suggest requiring the group engagement team to request their input as part of the risk assessment process and where deemed necessary in the design of further audit procedures, including where the group engagement team decides to perform these tasks centrally.

More generally, we are of the view that the introduction of the new risk-based approach proposed in ED 600 will require a substantial change in mind-set for auditors and the IAASB should consider what additional guidance can be provided to assist with this shift and to help auditors and audit firms to embrace the new mind-set. For example, the standard refers to the risk-based approach for determining the work efforts required to assess component auditors’ work, but it does not contain clear provisions on how that risk-based approach impacts the actual procedures to be performed by the group engagement team.

IRBA

The IRBA welcomes and supports the IAASB’s revision of the International Standard on Auditing 600, Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors) (ISA 600), which introduces an enhanced risk-based approach to planning and performing a group audit. This approach appropriately focuses the group engagement team’s attention and work effort on identifying and assessing the risks of material misstatement of the group financial statements, and on designing and performing further audit procedures to respond to those assessed risks.

We support the view that the risk-based approach will result in an appropriate assessment of the risks of material misstatement of the group financial statements and the design and performance of appropriate responses to those assessed risks, subject to there being enough guidance. Refer to our response to Question 8(c) for our concerns on the practical challenges that may arise from implementing the risk-based approach.

We submit that the wording in paragraphs 25 and 32 of ED-600 is incoherent. It is thus unclear what requirement in paragraph 32 must be fulfilled by the group engagement team from the current wording in paragraph 25. We recommend that paragraph 25 should rather refer to the principle of involving the component auditor in the understanding of the component’s system of internal control, with reference to the requirements of paragraphs 19 to 27 in ISA 315 (Revised 2019). In addition, paragraph 32 should then refer to the involvement of the component auditor in identifying and assessing the risks of material misstatement, with reference to the requirements of paragraphs 28 to 37 in ISA 315 (Revised 2019) (or ED-600 paragraph
31, as deemed appropriate), based on the understanding obtained by performing procedures referred to in paragraph 25 of ED-600.

**NASBA**

NASBA believes the risk-based approach in ED-600 should result in an appropriate assessment of the risks of material misstatement and appropriate response to the assessed risks.

NASBA would like to emphasize the importance of the group engagement team’s accountability for an appropriate assessment of the risks of material misstatement on a group audit. As recognized in ED-600, for the group engagement team to be successful, it has to have a thorough and complete understanding of the business including inherent risks, major processes and internal controls. NASBA believes this can be challenging in the larger and more complex group audits. ED-600 encourages component auditor involvement in assessing risks of material misstatement when the group engagement team considers such involvement appropriate. NASBA has some concerns regarding the possibility of insufficient involvement of component auditors resulting in an incomplete or inaccurate assessment by the group engagement team. The IAASB may want to consider providing more emphasis in ED-600 on use of component auditors for this purpose.

**4. National Auditing Standard Setters**

**CAASB**

Overall, we support the risk-based approach in ED-600. We believe this approach will focus the GET on planning and performing the group audit to address the risks of material misstatement at the group level. However, we believe further clarification or implementation guidance is needed in the following area.

Determining which components require risk assessment procedures and what those risk assessment procedures should entail

In the extant standard, for a significant component, a response may be to perform an audit of the financial information of the component, which is generally viewed as implying that a risk assessment using ISA 315(Revised) is performed. Under the risk-based approach in ED-600, the GET uses their professional judgment to determine when to involve a CA in risk assessment procedures and the nature and extent of the risk assessment procedures to assign to a CA. Due to the impact of the risk assessment process on the planning of the group audit, it is critical that the group risk assessment be robust and comprehensive. While paragraph A71 provides some factors that may influence the nature and extent of the risk assessment procedures assigned to a CA, some practitioners were not clear how these factors would influence the GET’s decision. For example, the paragraph does not explain how the nature of the components’ business activities and the group’s system of internal control can influence the GET’s decision regarding when to involve a CA in the risk assessment. Further, when the GET involves a CA in risk assessment procedures, paragraph A71 is unclear as to whether the risk assessment procedures would entail:

a “full risk assessment” under ISA 315 (Revised) for that component; or

if it is possible to only perform risk assessment procedures deemed necessary in the circumstances such as obtaining an understanding of relevant controls at the component level or making certain inquiries of component management.

Further clarification of these matters could be provided in paragraph A71 or in implementation guidance.
We recognize that some of these issues may be related to the transition from the extant to the revised standard. However, we believe providing implementation guidance on these topics would assist practitioners in gaining a better understanding of how to conduct a group audit under ED-600 and applying the standard consistently.

MIA

While it is important to indicate the importance of the GET’s accountability for an appropriate assessment of the risks of material misstatement on a group audit, for the GET to be effectively scoping the risks, it has to have a thorough and complete understanding of the business including inherent risks, major processes and internal controls. This can be challenging in the larger and more complex group audits.

The proposed approach may compromise audit quality as the GET may not identify and assess the risks of material misstatement at the component level, especially for those components with higher assessed risks of material misstatement that could result in risks of material misstatement at the group financial statement level, and may not be able to design appropriate responses to address those risks. As such, the IAASB could consider expanding paragraph A82 to reflect that component auditors should proactively relay potential risks of material misstatements to the GET.

NBA

The role of the component auditor (see Q8 in this letter)

The approach to risk identification and assessment, which aims to take a ‘top-down’ and more ‘horizontal’ view of the group. The group auditor has to undertake risk assessments of the components at a much more granular level, and with the change in approach to shift the accountability from the component auditor to the group auditor. We are of the opinion that the involvement of component auditors is critical. The changes seem to result in the component auditor involvement intended to be in a more piecemeal fashion;

A significant de-emphasis on the performance of an audit over the component financial information. The requirement for an audit for a ‘significant’ component is proposed to be removed. While we support a risk-based approach, we are of the opinion that it is very important to emphasize conditions where an audit is likely to be beneficial for audit quality. We recommend to make clear what the responsibilities of the component auditor are, especially related to reporting (e.g. whether an opinion of the component auditor is expected for the figures of the component).

5. Accounting Firms

BDO

Consideration of financial significance

The move away from the classification of components as financially significant and replacement by a wholly risk-based approach may have a detrimental impact on the information available to group engagement teams to make informed decisions about group risks of material misstatement (RMMs) and how they plan to respond to them at the group level. In our response to Question 8, we have proposed consideration of a stand-back mechanism to ensure the informational value attributable to financial significance is not overlooked within proposed ISA 600.
Notwithstanding the 'Matters of significant concern' we have identified on page 1, we are broadly supportive of the new risk-based approach as outlined in ED-600. From an audit and public interest perspective, there are clear benefits in having an updated approach to auditing groups that:

Builds upon and aligns closely with ISA 315 (Revised 2019) and extant ISA 330

Provides increased clarity about respective responsibilities (especially those of the group auditor)

Encourages the group engagement partner and wider group engagement team to focus on the nature of their role and the needs of the group audit, particularly through:

Identification and assessment of group RMMs

Seeing the group audit as an audit in its own right rather than a collection of smaller audits with top-up risk assessment or audit procedures performed purely for group purposes.

The new risk-based approach as set out in ED-600 has the potential to positively affect how both group and component auditors perform their respective roles and we support steps that can be taken to encourage more in-depth thinking about the nature of the risks affecting the group and how the group engagement team can best direct, supervise and/or review the work performed (whether by components or the group engagement team) for group audit purposes. We also recognize that the IAASB is having to wrestle with the practical challenge of outlining an approach to performing group audits in ED-600 that can reflect the disaggregated nature of a group (whether considering sources of data, management decision-making, accounting policies, location, etc.) while also emphasizing the importance of approaching the audit as if were a single entity engagement.

As noted in our 'Matters of significant concern', we are concerned that complete removal of the requirement for a significant component to have ‘…an audit of the financial information…’ or some element of consideration regarding financial significance may impact the information provided to group engagement teams. Potential impacts could include:

Creation of an overly-centralized approach that encourages group engagement teams to focus only on risks at the expense of other (financial) information about the group when making scoping decisions.

An inability to access valuable information from the audits of significant components (performed by a component auditor) that may have previously helped inform group engagement team identification and assessment of group RMMs.

As a result, we believe there may be a need for the IAASB to consider whether ED-600 needs some sort of stand-back mechanism (similar to how ISA 315 Revised has been developed). This stand-back may ensure that other factors may be considered by the group engagement team when identifying, assessing and responding to group RMMs (i.e., the horizontal scanning of risks across the group should be combined with a vertical consideration of significant classes of transactions and account balances in financially significant components). Our recommendation echoes a similar concern we raised at inception of the group audits project in our Invitation to Comment response in 2016.

One of the biggest challenges of auditing a group is the likelihood that there are multiple applicable financial reporting frameworks in operation across different components – which requires additional consideration by group engagement teams when planning their audit strategy. We note that ISA 315 (Revised) emphasized the importance of understanding the applicable financial reporting framework and our expectation was that this concept would have had more prominence within ED-600. Specifically, there should be more content for those situations (perhaps by way of application guidance) when component auditors are used by the group.
engagement team and the component auditor may (1) not be as aware or familiar with the group’s applicable financial reporting framework, or (2) the applicable financial reporting framework may be so different as to require more active direction, supervision and review by the group engagement team.

There are a number of additional practical impediments that could result in ED-600 not having the desired outcome as set out by the IAASB in their exposure draft. We have noted these impediments within each section below.

**BT**

The planning process under ED-600 looks like it will take longer than under the extant standard, even though you may end up with the same audit plan. We may see fewer full component audits, and more specified procedures, so some “big picture” view at a component level may be lost. There is also no “minimum floor” of work required on significant components. These two things together may result in less audit work being undertaken on the group under ISA 600 revised than is currently the case. The main driver behind revising ISA 600 was to improve the quality of group audits. Loss of big picture view and insufficient involvement of component auditors may not help with that and might result in a drop in audit quality.

Whilst it is clearly a good idea to involve component auditors in obtaining an understanding of the component and the risk assessment process at group level, there is no requirement to do so. The communication requirements are focused on the group auditor to component auditor direction, which is a missed opportunity to highlight the benefits of local knowledge that a component auditor brings to the group audit.

Yes. The division of responsibility for the risk assessment and responses are clear in the standard as is the ability to delegate the execution of the risk assessment and responses. Practically however, the removal of the significant component vs insignificant component guidance may mean that teams are less certain about which entities require audit procedures and which can be addressed with lesser procedures due to their size and nature.

**DTT**

DTTL believes that the risk-based approach appropriately builds on ISA 315 (Revised 2019) and will result in the group engagement team developing a group audit plan that addresses the nature, timing, and extent of the planned risk assessment procedures. DTTL also acknowledges that in certain circumstances, there may be practical challenges to implementing a risk-based approach, for example; in a complex group engagement structure in which there may be many sub-groups. However, DTTL believes that in these circumstances the practical challenges can be overcome when the group engagement team applies the principles in ED-600, including determining (1) whether the component auditor has the appropriate competence and capabilities and (2) the level of involvement in the work of the component auditor, including review of their work. DTTL believes that this, in combination with robust two-way communication with the immediate sub-group component auditors, and other component auditors as necessary based on the professional judgment of the group engagement partner, is foundational to executing a high-quality group audit. DTTL believes that application material addressing sub-groups explicitly may be appropriate, especially in the context of the group engagement team’s ability to direct and supervise, and assign risk assessment procedures to component auditors. DTTL recommends that the addition of “sub-groups” as an example in paragraph A71 of ED-600.

Obtaining sufficient appropriate audit evidence
DTTL notes that the objective in paragraph 8(d) of ED-600 is to “evaluate whether sufficient appropriate audit evidence has been obtained,” and as such DTTL agrees with the approach in the proposed standard to place greater emphasis on the identification and assessment of the risks of material misstatement at the group financial statement and assertions levels in accordance with ISA 315 (Revised 2019), including the resulting identification of significant classes of transactions, account balances, and disclosures and the relevant assertions at the group level, and the related response to those assessed risks as required by ISA 330, The Auditor’s Responses to Assessed Risks (referred to as the “risk-based approach”). In doing so, DTTL agrees with the determination by the Board to remove the extant concept of identifying a “significant component” for purposes of scoping a group audit and instead focus on obtaining audit evidence to address the assessed risk(s) of material misstatement, which may involve component auditors performing audit procedures on financial information of the component at the request of the group engagement team. DTTL therefore also agrees with the shift in the standards from a focus primarily on a rigid set of audit procedures required to be performed on components based on a high-level identification of their significance to the group, to applying the risk-based approach iteratively and flexibly and focusing first on the identification of the risks of material misstatement for the significant classes of transactions and account balances to the group (i.e., what work to perform), followed by determining the components where the work will be performed (i.e., where to perform the work), and ultimately identifying the members of the engagement team that will be performing the audit procedures (i.e., by whom; either the group engagement team or component auditors).

However, while ED-600 provides guidance on scoping a group audit (i.e., paragraphs A86-A93 of ED-600), the proposed standard provides only limited guidance related to considerations on determining the amount of audit work that is necessary to obtain sufficient appropriate audit evidence (i.e., paragraph 33 of ED-600, as well as the stand-back requirement in paragraph 49 of ED-600). DTTL is concerned that without providing factors for the auditor to consider, the auditor will find it challenging to make a determination that sufficient appropriate audit evidence has been obtained in a group audit and that audit risk has been reduced to an acceptably low level. DTTL strongly encourages the Board to more clearly articulate the special considerations related to the planned approach to obtaining sufficient appropriate audit evidence in a group audit (including application material related to the expected documentation of such considerations), including how such considerations are necessary when planning further audit procedures, as well as when evaluating whether sufficient appropriate audit evidence has been obtained. Without this, there is the potential for vast differences in the nature and extent of audit evidence that is obtained in a group audit, including for group audits in which there would be an expectation of general consistency in the nature and extent of evidence obtained.

DTTL notes that paragraph A62 of ISA 330 includes various factors that may be considered when concluding that sufficient appropriate audit evidence has been obtained. DTTL believes that this can be used as a starting point for determining the special considerations in a group audit, in addition to the following concepts:

The nature and amount of classes of transactions and account balances in the group financial statements, and the transactions that are executed at the entities or business units that comprise the group, including the related risks of material misstatement and the commonality of risks across the entities or business units.

The materiality of the entities or business units that comprise the group, as well as the materiality of the components selected for testing.

The nature and extent of audit evidence obtained for significant classes of transactions and account balances.
The effectiveness of the control environment, including the commonality of controls, the information technology (IT) systems, and the monitoring activities by the group as it relates to the entities or business units comprising the group.

EYG

As commented in our response to the IAASB Invitation to Comment on Group Audits, we are supportive of a risk-based approach to planning and performing group audits focused on the risks of material misstatement of the group financial statements. We believe that under such an approach the auditor will be able to better demonstrate how the group audit is responsive to the risks of material misstatement identified in the group financial statements, which will in turn better facilitate and support the auditor’s conclusion that sufficient appropriate audit evidence has been obtained. We therefore believe it would result in improving the quality in group audits by the engagement team spending time and effort where it matters the most. However, we do not think the current draft of the risk-based approach in ED-600 will be successful in achieving the desired outcome of enhancing quality in group audits because of many practical challenges we see in its implementation.

Our views are informed by our field testing activities that focused on ED-600 paragraphs 31 to 39. Feedback was collected from a wide range of population around the world, from teams auditing medium to very large groups; approximately 20 audit teams that represented 12 Regions or countries were involved.

Significant concerns and questions have been raised through our field testing activities, which are explained in detail by themes below. We therefore think it is critical that the IAASB responds to these points in its revisions to ED-600, so that the risk-based approach can be scalable – particularly up- and operationalizable for all groups.

We recommend the IAASB particularly take into account that component auditors may be from a different firm, or network, from the group engagement team and therefore not subject to the same interpretative guidance issued by the group engagement team’s firm. It is therefore important that ED-600 provides a foundation for consistent operation across all firms.

Risk-based approach, including scalability

We support a more flexible risk-based approach to scoping a group audit and are supportive of the proposals to require additional focus on the group engagement team’s considerations when understanding the group and its environment as well as when identifying the applicable risks of material misstatements of the group financial statements. We do however have significant concerns with the proposed approach in ED-600 and in particular for larger size and more complex groups. As currently drafted, ED-600 could lead to many different interpretations of the standard, it does not currently offer a strong framework for identifying components and allocating work that would allow auditors to apply the standard consistently and it is lacking practical solutions and examples on how the new requirements are to be implemented in different scenarios.

Our response to Question 8 includes specific suggestions for a framework for determining components, involving component auditors, and determining the allocation of work to component auditors.

While we fully support an approach where the group engagement team is ultimately responsible for the group audit and has overall responsibility for the planning and execution of the group audit, we believe ED-600 does not provide a balanced perspective on the important role of component auditors. It is necessary for the group engagement team to leverage the knowledge and expertise from component auditors related to local laws and regulations, the control environment and internal control at the component, and any other risks that cannot be effectively addressed at the group level. In particular, we believe that component
auditors are critical to identifying and addressing risks of fraud at the component level. Refer to our responses to Questions 3 and 8 for further details regarding our concerns, and potential unintended consequences, of ED-600 underplaying the role of component auditors.

GT

Overall, we are of the view that the proposed risk-based approach can result in an appropriate assessment of the risks of material misstatement of the group financial statements. Our concern lies with the apparent lack of flexibility in the proposals and with whether the proposals allow for sufficient use of the component auditor, which is both effective and efficient, in the proposed approach. A number of the practical challenges posed by ED-600 highlighted in our response to part (c) of the question, either arise when, or are exacerbated by, a firm using another firm outside of its network as a component auditor in a group audit engagement. This is of particular concern for smaller firms that specialise in providing component auditor support to larger firms because of jurisdictional or cultural differences. As we indicated in our overall comments, we do not believe that creating requirements that may create competitive disadvantages is in the public interest.

Overall, we are supportive of the efforts to revise extant ISA 600 in response to the issues identified through the IAASB’s Invitation to Comment: Enhancing Audit Quality in the Public Interest – A Focus on Professional Skepticism, Quality Control and Group Audits (the ITC).

In particular, we are supportive of the intent to provide increased flexibility in scoping a group audit through the introduction of a different risk-based approach (a “horizontal approach”) to scoping. In comparison to the approach in extant ISA 600, which primarily focuses on scoping by component (a “vertical approach”), we are of the view that this horizontal approach has the potential to enhance audit quality through an improved focus on the risk of material misstatement at the group level taking into account the requirements of ISA 315 (Revised) related to classes of transactions, account balances and disclosures that comprise the group. For firms that are currently not applying a horizontal as well as a vertical approach, this may promote an appropriate risk assessment and related response to obtain sufficient appropriate audit evidence to express an opinion on the group financial statements.

However, we are of the view that, as drafted, ED-600 doesn’t convey the intent to allow the level of flexibility necessary to scope and perform the most effective and efficient group audit (that is, the ability to scope group audit engagements in both a horizontal and a vertical manner is not evident in the current proposals). A combined approach not only takes into account both the risk associated with the financial statement line item and the component in which that risk resides, but also allows for the group engagement team to modify the approach to the group engagement based on the source of that evidence. The lack of emphasis on the vertical approach (that is, considering the significance of components as well as statutory or local audit requirements) may result in a loss of a more holistic group audit approach, which may, in turn, have a detrimental effect on obtaining sufficient appropriate audit evidence as well as the ability to conduct the group audit within a reasonable period of time and at a reasonable cost. In addition, we are not clear how the proposals in ED-600 are intended to change a firm’s current use of a combined approach and if there will be benefits to such a change.

We have highlighted below several concerns with the proposals in ED-600, on which we further elaborate in our detailed response in Appendix A.
However, we believe it is important that the proposed standard provide additional clarifications/implementation considerations, in order to fully achieve its overarching objectives. These relate to certain aspects of the application of the risk-based approach, in particular, on larger and more complex group audit engagements, in respect of which we believe it likely that more extensive involvement of component auditors would be necessary, recognising their important contribution to enable the group auditor to obtain sufficient appropriate audit evidence in respect of the group as a whole. In particular, we are concerned that the proposed standard appears to de-emphasise the role that an audit of component financial information may have in assisting the group engagement team with meeting their responsibilities, as an audit provides a robust framework setting out a component auditor’s responsibilities with respect to the work to be performed over the financial information of a component at the direction of the group engagement team. The proposed standard, as drafted, may not give sufficient prominence to the important role and responsibilities of the component auditor and therefore we make certain recommendations regarding clarification of the proposed standard.

De-Emphasis of an Audit of Component Financial Information

We recognise that the proposed standard continues to contemplate the involvement of component auditors both by emphasising that they are part of the group engagement team and by including commentary in the application material regarding their “more in-depth knowledge of the component” (A96), and “their direct knowledge and experience with the entities or business units” (A79).

However, we are concerned that an audit of the component financial information as an appropriate response appears to be somewhat de-emphasised in the revised standard. (Please refer to our response to Question 8 for further details).

We understand the Board’s observations, as described in paragraph 48 of the Explanatory Memorandum (EM), that the extant standard may result in the group engagement team “defaulting” to an audit of the component financial information and concerns regarding possible “over-reliance” by the group engagement team on such an audit. Accordingly, we recognise the Board’s intention, in the revised standard, to drive the group engagement team to focus on whether and how the assessed risks of material misstatement of the group financial statements are properly identified and addressed and to avoid “blind reliance” on the work of the component auditor.

However, we believe that an audit, performed by a component auditor, is often an appropriate solution from an audit quality perspective. This is because the component auditor performs an audit, which is a clearly defined and understood engagement type and which is required to be performed in compliance with all other ISAs, as relevant. It provides a robust framework for a component auditor’s responsibilities with respect to the work to be performed at the direction of the group engagement team, including communication with the group engagement team. These features do not diminish the responsibilities of the group engagement team. Instead, they help to ensure that the component auditor is clear as to their remit and takes appropriate responsibility for their involvement, which may be critical in view of the underlying reasons for their involvement.

As a result, we suggest that the application material expand on the current content, regarding the component auditor’s knowledge and experience, to clearly explain the reasons as to why it may be optimal, from an audit quality perspective, to perform an audit over component financial information in certain scenarios.
When to Involve a Component Auditor

In connection with the above, we recommend that the standard provide further clarity as to when it would be appropriate/ optimal to involve a component auditor, including greater acknowledgement that using the work of a component auditor may result in a more effective approach both to identifying and assessing risks and obtaining sufficient appropriate audit evidence, building on the material already included. This would be an enhancement over the extant standard, which is focused only on whether a group auditor may use the work of a component auditor.

To reinforce the importance of this, we suggest the establishment of a requirement for the group engagement team to update their preliminary considerations regarding the involvement of a component auditor, e.g. at paragraph 21, as part of considering whether the group engagement team overall (including component auditors) has the appropriate competence and capabilities to perform the group audit.

How to Involve a Component Auditor

Whilst we recognise the IAASB’s rationale for removing the binary classification of components as significant or non-significant and the resultant prescriptive responses, we recommend that the application material describe the different ways to involve a component auditor in terms of the nature, timing and extent of their involvement in performing procedures and, furthermore, that the standard provide a framework, including factors that the group engagement team would consider in making the determination as to how to involve a component auditor.

In order to formalise such considerations and give appropriate prominence to their importance, we also suggest the establishment of a requirement for the group engagement team to determine how to involve a component auditor, linked to this guidance. Furthermore, we suggest that the Board consider whether to extend this to explicitly include consideration as to whether it would be appropriate to request a component auditor to perform an audit of the component financial information, or a part thereof, as we describe above.

We recognise the significant work effort of the IAASB with respect to this project to date and we are supportive of the Board’s overall aim to ensure that the standard remains fit for purpose. We support, in particular, the enhancements made by the introduction of the new “risk-based approach”, which we consider will help drive greater focus by the group engagement team on their responsibility to identify and assess the risks of material misstatement of the group financial statements and to design and perform further audit procedures to respond to those risks, in order to obtain sufficient appropriate audit evidence in respect of the group audit as a whole. This is a fundamental responsibility of the group auditor and therefore we welcome the increased emphasis placed on this within the revised standard.

We support the development of the risk-based approach, in particular, to drive greater focus by the group engagement team on their responsibility to identify and assess the risks of material misstatement of the group financial statements and to design and perform further audit procedures that are responsive to those risks, in order to obtain sufficient appropriate audit evidence in respect of the group as a whole.

MAZ

While we understand that a top down approach can be useful, we believe that not involving component auditors does not enable the group auditor to have an efficient risk assessment and does not favour professional scepticism when gathering audit evidence. Application material shows implicitly a combined approach (Top-down approach starting from the group financial statements combined with the extant practice of the decision tree Significant-non-significant components). We believe that the combined
approach should be more explicitly referenced in the main body of the standard to avoid misinterpretation and underutilization of the component auditors in performing the audit.

We believe that one key success factors for audit quality in a group audit is an effective and efficient two-way communication between the Group auditor and the component auditors. We think it should be more highlighted in the standard.

MGN

The top down approach taken by the proposed revised ISA has much to recommend it, however we do have some concerns. The pivot away from ‘significant components’ does make perfect sense in many contexts, but possibly not in all. We suggest that it might be more ‘scalable’ if IAASB considers whether a hybrid approach could be adopted which takes more into account the nature and circumstances of a group, and indeed of the group auditor and which would enable a significant component approach in specific circumstances where that would be appropriate and suitable in context. Allowing such an approach would necessitate additional guidance on what auditors should consider (and document) when determining which approach was suitable.

An alternative to the above could be considering simply providing more guidance stressing that the nature and circumstances of a group are a key consideration to determining the approach taken and including an example in the guidance which illustrates when that might lead to a more traditional component audit (at least partially). An allowable hybrid approach might reduce the potential lack of proportionality between the impact of the revisions and improvements in audit quality in some circumstances. While we note that appendix 1 contains material relating to component auditors, we feel that guidance could be more prominent.

The proposals do not require a minimum level of local risk assessment. This could give rise to the risk that, if component auditors are less involved (or are no longer used in some cases) the group engagement team may not obtain the information they need to identify and/or assess locally derived relevant risks.

We support the general principle of a risk-based approach. We believe that the risk-based approach will generally result in appropriate assessments of risk and design and performance of risk responses. However, we have concerns that the increase in the level of additional process that may be required may not be matched by a proportionate improvement in audit quality outcomes

PwC

Overall

We believe the standard lacks sufficient clarity regarding the group engagement team’s thought process and practical considerations in making key judgements when determining the overall group audit strategy and involvement of component auditors. Further explanation is needed of what it really means in practice to “take responsibility” for the key judgements around scoping, risk assessment and design of responses, while recognising the vital role component auditors play in most group audits.

Paragraph 50 of the explanatory memorandum outlines the Board’s view of how the risk-based approach to a group audit can be characterised, highlighting the judgements that need to be made about what, how, by whom, and where audit procedures will be performed in the group audit. Such judgements necessarily need to be based on a preliminary understanding of how management views and controls the business, taking into account the group, its structure, its financial reporting processes and system of internal control.
Our response to question 6 includes our recommendations for enhancing the requirement for understanding the group and provides additional factors for group engagement teams to consider when identifying components.

Understanding the group structure, financial reporting processes and relevant controls is also important in determining how best to approach a group audit and the key judgements that need to be made around the involvement of component auditors in both risk assessment and performing further audit procedures to respond to risks of material misstatement.

For some engagements, approaching the audit by focussing in the first instance on the classes of transactions, account balances and disclosures that are significant to the group financial statements (SCOTABD) works well. For others, a continued focus on significant components first may remain the best approach (e.g., when there are specific or unique risks associated with a location or business unit). In practice, we anticipate the processes to scope a group audit, understand potential risks of material misstatement to the group financial statements, and designing appropriate responses to those risks will be an iterative process, rather than a linear one.

In addition to the factors we describe in our response to question 6 that assist group engagement teams in deciding where to perform work (identifying components), we believe it is important that the proposed standard provides more guidance on further factors that should be considered by the group engagement team in determining the most effective approach to the group audit, including the nature and extent of involvement of component auditors in risk assessment and responding to identified risks. This should also include additional guidance to address both the circumstances when a full-scope audit may be warranted, and those in which more targeted audit procedures may be appropriate. For example, a decision to request a full-scope audit of a component that is “financially significant” to the group would not be uncommon. Such guidance would benefit group engagement teams in making consistent judgements.

We therefore recommend that the standard includes an overarching new requirement based on ISA 300 paragraph 7 addressing the special considerations in developing the overall group audit strategy that sets the scope, timing and direction of the group audit. Application material to this requirement can include the factors referred to in the preceding paragraph.

The factors set out in paragraph 12 of the PCAOB’s AS 2101 could help provide a useful starting point for this judgement framework, which could be expanded to address factors that, as suggested, may indicate that a full-scope audit may be warranted. We believe this would lead to greater consistency in judgements in relation to aggregation risk, which is another objective of the IAASB.

Proposals need to be strengthened to maintain group audit quality

Current ISA 600 provides a framework for determining where audit work needs to be performed, through the requirement for an audit of individually financially significant components together with ensuring appropriate focus on addressing significant risks of material misstatement of the group financial statements at components. This framework was intended to serve as a safeguard to the sufficiency and rigour of audit work that is necessary across the group to provide a basis for the opinion on the group financial statements. This approach provided several benefits:

It helped promote consistent understanding about where work should be performed.

It ensured a focus on complying with all of the ISAs, including risk assessment procedures by component auditors at those components where a full-scope audit or an audit of one or more account balances, classes
of transactions or disclosures was performed. This component auditor involvement helped avoid risks of material misstatement ("risks") being missed at the component level that may be relevant group audit risks. It embedded an additional layer of responsibility for managing quality at those components through the responsibilities of the component engagement partner. As a basis for forming an audit opinion on some or all of component financial information, the component auditor was responsible for the appropriate direction, supervision and review at the component level due to the applicability of ISA 220 to that audit work.

The additional layer of accountability at the component auditor level did not in any way reduce the group engagement partner’s overall responsibility for the group audit and judgements made around risks, responses and sufficiency of evidence. But it embedded another level of shared accountability for audit quality with those best placed to contribute to it.

Changes in organisational and financial reporting structures have introduced challenges in applying extant ISA 600 in some circumstances, and we are not proposing to retain the status quo. But in moving away from the framework in extant ISA 600 that guided the scoping judgements in the group audit, it is vital that the proposed standard provides an equivalent framework to guide auditors in making appropriate decisions in the circumstances about the sufficiency and appropriateness of work performed across the group. We do not believe the current proposals achieve this.

We support a risk-based approach to a group audit, built around principles-based requirements, that enables the group engagement team to approach scoping of the group audit as best suits the group’s organisational and financial reporting structure. However, we believe there are potential risks, drawbacks and challenges to the approach as currently described in the proposed standard. Without further changes, we do not believe the current proposals provide a sufficient framework to maintain audit quality.

6. Public Sector Organizations

GAO

The risk-based approach has the potential to result in an appropriate assessment of the risks of material misstatement of the group financial statements and the design and performance of appropriate responses to those assessed risks. We believe that a practical challenge may be with the two-way communication between the group auditor and the component auditor. However, we are concerned that there may be instances where the group auditor does not assign the design and performance of risk assessment procedures to a component auditor, but the component auditor nonetheless is aware of risks that may impact the group audit. We believe this can be addressed by providing an additional example in 44 (g) or an additional sub-sentence in paragraph 44 that discusses communication of risks to the group auditor. In addition, we suggest clarifying whether paragraph 44 is referring to all the component auditors or just the component auditors involved by the group auditor in the audit.

7. Member Bodies and Other Professional Organizations

AE

Similarly, the top-down approach could, if not applied appropriately, reduce the ability of the group team to have a proper risk assessment and identification. Should the group engagement team perform the audit without component auditors as a systemic answer, in some cases, it could be detrimental to the quality of the audit. We elaborate on this issue in our response to question 8 and propose a way to address it.
The Exposure Draft ISA 600 (ED-600) addresses relevant areas that, in our view, needed to be reconsidered when conducting group audits. In this regard, keeping in mind the intricacies of establishing a globally accepted set of requirements for a wide range of scenarios, we support the revision of the extant ISA 600 in a way to emphasize a risk-based audit approach to group audits.

Including more flexibility and agility than the extant ISA 600 will result in the standard being more responsive to the audits of both simple and highly complex groups of entities, as well as making it more future proof. These attributes should be kept in the finalised version.

Yes, in principle, we believe that the risk-based approach to group audits will result in appropriate risk assessment. Although this is an application issue, we are concerned that it may lead to more procedures without necessarily improving audit quality outcomes.

Additionally, in line with our earlier comments, it has potential implications to a lesser extent of involvement of component auditors in group audits. Hence, some risks of material misstatement may not be brought up and may therefore be missed at the group level. It would be helpful to emphasise the need for sufficient local knowledge that may be needed to better understand the components and their operating environment.

Similarly, the top-down approach could, if not applied properly, reduce the ability of the group team to have a proper risk assessment and identification. Should the group engagement team perform the audit without component auditors as a systemic answer, in some cases, it could be detrimental to the quality of the audit (i.e. lacking full information for risk identification and assessment). With this in mind, we believe that, for groups involving components with differing languages, cultures, laws and regulations, and business practices, the group engagement team should be required to consider the need to involve component auditors and to revise their preliminary determination made in accordance with paragraph 13 as necessary. Consequently, the group auditor’s strategy regarding the extent of involvement of component auditors is of such significance that the rationale supporting their strategy should be properly documented.

Finally, as emphasised in our cover letter, this approach might have the counterproductive effect of discouraging the involvement of component auditors, especially when they are not in the same network. We fear that this could have implications on the audit market and the level of competition in some countries in Europe. The significance of this risk very much depends on the jurisdiction and on the complexity of group audits that are considered.

**CAANZ-ACCA**

Risk-based approach

We support the concept that the risk assessment should be driving the work effort for the group audit building from the risk-based approach introduced in 315 (Revised) rather than the extant ISA 600 concept referring to the significance of components. However, there are significant concerns raised by SMPs that since the risk assessment will be performed by the group engagement team without the involvement of component auditors, this could impair audit quality as the involvement of component auditors often bring local knowledge and expertise.

We support the concept that the risk assessment should be driving the work effort for the group audit building from the risk-based approach introduced in 315 (Revised) rather than the extant ISA 600 concept referring to the significance of components. However, there are significant concerns raised by SMPs that since the risk assessment will be performed by the group engagement team without the involvement of component auditors, this could impair audit quality as the involvement of component auditors often brings local knowledge and expertise.
CPAA

With regards to the appropriate assessment of the risks of material misstatement in a group audit, ED-600 makes clear that the group engagement team has to have a thorough understanding of the inherent risks and internal controls of the business. We believe that in larger and complex group audits this can become especially challenging. We are concerned that insufficient involvement of component auditors may lead to incomplete and/or inaccurate risk assessments by the group engagement team. By not requiring component auditors to undertake full-scope audits of “significant components”, as defined in the extant standard, this may lead to component auditors not being able to adopt a holistic audit approach to a component. For complex audits with many components, it will be particularly challenging for the group engagement team to be able to identify all of the risks arising from the group’s components and operations.

We note that the ED places a greater onus on the group engagement team in the conduct the group audit, with less reliance on audits of component financial statements in their entirety. This will present a potentially significant challenge for group engagement teams when the group includes many components, is geographically spread and/or comprises a complex structure. The approach, if managed well, should result in a more targeted approach as it will be driven by the risk assessment, which is intended to improve audit quality, and may also result in some efficiency gains. However, there are also risks which arise from potentially less involvement of component auditors. If the component auditors’ involvement is diminished in circumstances where they hold specific knowledge and understanding of the components, which is not fully appreciated or leveraged by the group engagement team, audit quality may be compromised. Therefore, we recommend strengthening the requirement to consider the appropriate involvement of the component auditor and the measures to integrate the component auditor into the engagement team. For example, this can be done by the group engagement team sharing its risk assessment with component auditors and inviting input on that assessment and the planned responses to assessed risk. This would ensure that component auditors are not operating in isolation of the overall audit approach.

We note that ED-600 was released prior to the outbreak of COVID-19 and, therefore, does not take into consideration the changing circumstances currently experienced by the auditing profession, in particular the worldwide shift to remote working and the technological solutions which have enabled the rapid implementation of new ways of working. These new ways of working are likely to endure to some degree into the foreseeable future. Whilst the shift to technology-enabled audits had been gaining momentum prior to the pandemic, there has been a significant acceleration in this shift. Audit firms of all sizes are exposed to increased pressure to adopt digital transformation strategies and to implement technological tools. Looking forward, we expect increasing levels of remote auditing and automated, or at least technologically enabled, audits. Therefore, we encourage the IAASB to provide more application material addressing the undertaking of remote auditing in the context of group audits.

EFAA

We generally support a risk-based approach to the audit of the group financial statement.

Specifically, the removal of the requirement for an audit of significant components and allowing the group engagement team (GET) to elect to perform all the risk identification, assessment and response procedures without recourse to component auditors – a top down approach - may impair the quality of the audit of the group financial statements. The GET’s election may arise from its over optimism in its ability to perform the risk assessments on its own. In the absence of component auditors of significant components performing an
audit, we fear that the risk identification and assessment procedures for certain classes of transactions, account balances and disclosures may be less effective and adversely impact the design and performance of risk response procedures. Therefore, we believe appropriate safeguards, perhaps in the form of additional requirements, may be necessary so as to ensure that the GET is motivated to obtain sufficient knowledge of significant components, typically via the component auditor’s involvement.

We also suspect that the proposed top-down approach may lead to group auditors either reducing their reliance on the work of component auditors or selecting different component auditors for the group audit than at present. Group auditors may prefer to have their own firm or network be the component auditor not least because of familiarity and practical simplicity. This may result in fewer SMPs being engaged as component auditors.

On the one hand, adoption of the risk-based approach is intuitive and aligned with ISA 315 (Revised): risk assessment should be driving the work effort of the audit rather than whether the component is significant. On the other hand, removal of the requirement for an audit of significant components and allowing the GET to elect to perform all risk identification, assessment, and response procedures without recourse to component auditors could be detrimental to audit quality of the group audit statements. Moreover, in certain instances it may be more efficient for the component auditor to perform the risk assessment and design procedures to address the risks, and then have those reviewed and approved by the GET. That is, it may be more efficient and effective to audit the financial information of the component in its entirety, rather than designing and performing further audit procedures, which may not cover all of the information of what used to be called a component and thus, potentially impacting the quality of the group audit engagement.

FAR

In general, FAR supports the response submitted by the Nordic Federation of Public Accountants and FAR therefore refers to this response.

ICAEW

We note the move away from the classification of ‘significant’ components, the revised definition of a component and the top-down risk-based approach proposed in ED-600. We do not object to these changes in principle but in practice they are likely to result in increased audit effort and cost through the performance of additional procedures and there will be practical implementation challenges. Respondents to our enquiries have questioned the extent to which such an approach will improve audit quality outcomes. In particular, there are concerns that the approach might discourage or change the nature of the involvement of component auditors in group audits, impacting the relationship between the group engagement team and component auditors such that risks of material misstatement relevant to the group financial statements may be missed.

Where component auditors are involved in the audit of the group financial statements, there will be practical implementation challenges for the group engagement team in implementing ED-600. These relate to how they approach the risk assessment and the extent, nature and timing of communications with component auditors and will affect all aspects of the audit process. Significant effort will be needed at the planning stage of the audit and this needs to be clearly communicated in implementation support materials.

The responsibilities relating to client acceptance in ED-600 appear to be rather circular which might lead to confusion when trying to decide at what stage the group engagement team should involve component auditors. For instance, ED-600.13 requires the group engagement team to obtain sufficient understanding of the group to identify components and decide whether to involve component auditors. The related application
guidance gives a number of ways this might be done. However, as A24 says, there may be cultural or translation issues in doing this for some parts of the group. The most logical way to resolve this might therefore be to talk to the component auditors at this stage, even if the group engagement team is not going to involve them in all of the subsequent audit.

While we do not object to these changes in principle, in practice they are likely to result in increased audit process and practical implementation challenges for what may be questionable benefit.

While respondents to our enquiries agreed that a top-down approach, which focuses on the group engagement team’s responsibility to identify and assess the risks of material misstatement of the group financial statements and to determine the work effort that is needed to respond to the assessed risks, is important, it is not without its own risks to audit quality, as outlined below.

**IPA**

Risk Based Approach to Identification of Audit Components – while we support the introduction of risk-based approach in ISA 600, we are concerned that the linkage of the existence of group audit to consolidation entries (in particular elimination entries) and the application guidance on centralised accounting functions are inconsistent with such an approach and would result in inappropriate outcomes

**ISCA**

However, we are concerned that the revised approach to risk identification and assessment, which requires the group auditor to take a “top-down” and more “horizontal” view of the group audit overall, with very granular upfront involvement, is likely to be challenging. Below are our views on some of the practical challenges.

**KICPA**

In addition, the risk of material misstatements of group financial statements should be identified, not only from the perspective of the group auditor (top-down) but from that of component auditors (bottom-up), which would result in sufficient assessment of audit risks of group financial statements. Given this, more clarified and specified definition on the role and responsibility of group auditors should be provided, as we believe.

**MICPA**

With reference to Paragraph 52 of the proposed ISA 600 (Revised), whilst it is important that the group engagement team remains responsible for the identification, assessment and responses to the risks of material misstatement of the group financial statements, we are of the view that this can be quite challenging in the larger and more complex group audit engagements. This is because for an effective scoping of the risks, there has to be a thorough and complete understanding of the business and operations of the components including full familiarity of the local risks and regulatory environment.

**NRF**

In general, we support the risk-based approach to planning and performing the audit of the group financial statements.

However, we do have some concerns about the proposed top-down approach. In our view, allowing the Group Engagement Team (GET) to perform all risk identification, assessment and responsive procedures
without necessary recourse to component auditors, not even to those auditing significant components, might lead to less involvement of component auditors which, in turn, might affect the audit quality.

In principle we believe that a risk-based approach to group audits should result in appropriate risk assessments.

However, the risk-based approach in ED-600 is combined with a more centralized and top-down way of working, including more focus on the responsibilities of the GET, especially with regard to direction, supervision and review. Even though we support the emphasis of the group auditor being more involved, we are not convinced that the suggested structure and way of working, which will require more focus and work on team performance – and not on the group audit itself – necessarily will increase audit quality.

Regarding the involvement of component auditors in group audits, we believe that the requirements and application material in ED-600 might be a bit unbalanced in that it focuses very much on additional requirements related to the direction, supervision and review of component auditors, without also emphasizing the benefits of using these in the group audit in order to enhance audit quality.

SAICA

SAICA welcomes the introduction of the risk-based approach. This approach requires the group engagement team to obtain an understanding of the group structure and to determine components as well as to identify significant risks at the group level. This is consistent with the requirements in ISA 315 (Revised 2019) and the responses to the assessed risks of material misstatement are aligned to the requirements of ISA 330.

The risk-based approach, however, also poses the risk that significant risks at the component level may be overlooked. Where similar risks exist across all other components, this could have a significant impact on the group audit opinion. In this regard, an additional application paragraph following after A79 of ED-600 could be included to emphasise this point. The application paragraph should specifically require the group engagement team to remain alert to this scenario and design appropriate audit procedures to address this risk.

The introduction of the risk-based approach is aligned to the requirements of ISA 315 (Revised 2019), Identifying and Assessing the Risks of Material Misstatement, and instead of a preoccupation with identifying significant components, the risk-based approach should lead to an appropriate assessment of risks at group level and eliminate scenarios where detailed procedures are performed at components that have limited significance to the audit group opinion. However, as this is a new approach, significant guidance needs to be provided to ensure that there is some level of consistency across all group audits and that firms do not develop audit methodologies that are too divergent or even contradictory. SAICA is of the view that there is room for improvement in this regard. Refer to our response in Question 8(a) to (c) below.

SMPAG

We have different views on this area, stemming from different perceptions of the diverse circumstances of group audit constructs and different legal environments. ED ISA 600 proposes a top-down approach that will work well in many group audit circumstances – especially where the entire group is within a single jurisdiction, but it may be less appropriate for larger geographically spread groups.

Some practitioners believe that the proposed removal of the requirement for an audit for significant components and allowing the GET to elect to perform all risk identification, assessment and responsive procedures without recourse to component auditors could be detrimental to audit quality of the group
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financial statements, especially in respect of larger geographically spread groups. In addition, in certain cases it could be more efficient for the component auditor to perform the risk assessment and design procedures to address the risks, and then have those reviewed and approved by the GET. Indeed, e. in some circumstances, it might become more efficient and effective to audit the financial information of the component in its entirety, rather than have the GET designing and performing further audit procedures, which may not cover all of a specific component’s financial information, potentially impacting the quality of the group audit engagement. Especially where the component is “significant” in terms of extant ISA 600.

Other practitioners are very supportive of the enhanced risk-based approach. They believe that this is in alignment with ISA 315 (Revised), especially with the removal of identifying significant and non-significant components. They are supportive of the fact that the risk assessment should be driving the work effort for the audit, rather than how significant the component is as in the extant. The SMP AG agrees that the proposed top-down approach should be appropriate in many group situations possibly other than in respect of larger geographically spread groups.

In addition, some have observed that there can currently be an inconsistent approach to the audit of components by group auditors, even when the component is relatively large as part of a group. In practice the use of the term “significant component” can be poorly understood and inconsistently used. While there are some suggestions in extant ISA 600 as to how this may be defined (for example 15% of a chosen benchmark), it is still for the GET to decide what benchmark or percentage is appropriate.

In conclusion, and as explained in response to question 2 above, the SMPAG urges the Board to develop a mechanism to ensure audit quality will not be compromised by potentially less-well-informed decisions as to the involvement of component auditors.

Q8 – Disagree

4. National Auditing Standard Setters

CNCC-CSOEC

We consider that with a top-down approach, as proposed in the ED-600, the group engagement team may not identify certain risks that can only be identified locally, especially risks related to tax, fraud or going concern. For example, if there is a problem in the local market with potential impact on the group’s going concern, the group may not be aware of it. We therefore recommend that the IAASB emphasize the importance of having sufficient local knowledge to obtain an appropriate assessment of the risks of material misstatement of the group financial statements.

We understand the objectives of the revision of the extant ISA 600 as a way to encourage a risk-based audit approach to group audits. However, we would like to highlight some serious concerns we have about the proposed ISA (ED-600):

- Centralised approach vs approach by components

The centralised approach, as prescribed by the ED-600, appears to be systematically favored as the privileged route to audit group financial statements. We believe in some cases, especially for complex groups, an approach using component auditors may be better and more efficient. A pure centralised approach bears the risk of reducing the ability of the group engagement team to properly identify risks of material misstatement and to exercise its professional skepticism with respect to the group financial statements. Because the group engagement team will have as its main source of information, the group management, it will not be able to corroborate the information obtained with other sources of
Information it would have obtained from the component auditors. We therefore consider that the ED 600, which main element of scalability is the possibility given by the ED not to use component auditors, can make it inappropriate for larger complex group audits. Scalability should work towards less complex situations but also towards more complex situations. We believe that ED-600 is scalable to audit smaller, simpler groups but not to audit larger, more complex groups. We recommend to add a requirement in the ED for the group auditor to justify the appropriateness of the decision to use or not use component auditors.

IDW

However, in this letter we would like to make a number of important overall observations. Although we support revising ISA 600 to improve audit quality on group audits – in particular by improving the involvement of the group engagement team in the work of component auditors and improving the identification and assessment, and response to, the risks of material misstatement of the financial information of components that are not significant individually but are so collectively – we are not convinced that some of the key measures and approaches proposed in the draft will be conducive to increasing the quality of group audits, and believe that the draft may be impracticable to implement in a range of circumstances and may have detrimental effects on the audit market. Without addressing all of the major issues that we have identified in our response in Appendix 1 to the questions posed in the Explanatory Memorandum, we address the overriding issues that we believe have the potential to significantly decrease audit quality below.

We believe that the risk-based approach as proposed in the draft, which includes a top-down approach with micromanagement of the work of component auditors through the specification of procedures (whether risk assessment or risk response) and the application of technology for “remote auditing” will mislead group engagement teams into seeking to increasingly perform audit work on components without using the work of component auditors in situations in which group engagement teams may not be able to do so effectively. These situations arise primarily for components in jurisdictions with significantly different laws and regulations, cultures, languages, and business practices. Furthermore, we believe that eliminating the concept of significant components due to their financial size, together with the elimination of the concomitant requirement to have the entire financial information of those significant components subject to a full-scope audit, will increase the risk that material misstatements (in particular, those resulting from fraud, non-compliance with laws and regulations, and going concern issues at component level) of the group financial statements at component level will not be detected and will therefore reduce audit quality. We also believe that the approach as proposed does not adequately clarify 1. when component auditors are to be involved, 2. if they are to be involved, the nature, timing and extent of their involvement and 3. the nature, timing and extent of the involvement of the group engagement team in the work of component auditors. We provide suggestions as to how these matters can be addressed in our responses to Question 8.

We also believe that the risk-based approach as described in the draft will be difficult to implement in practice because of the granular risk assessment required by ISA 315 (Revised 2019) and ISA 540 (Revised) and the more granular risk response required by ISA 540 (Revised), which will cause a great increase in the extent of communication required between group engagement team and component auditors. Communication between group engagement teams and component auditors from another firm or network that are subject to different quality management systems and use different audit methodologies and tools would become particularly difficult.

We would also like to point out that a risk-based approach as described in the draft will also lead to undesirable effects on the audit market. In particular, the approach will lead to group engagement teams
seeking to only use component auditors from within the same firm or network because the granular risk assessment required by ISA 315 (Revised 2019) and ISA 540 (Revised) and the more granular risk response required by ISA 540 (Revised) will lead to more granular direction, supervision and review and therefore increase pressure to use component auditors subject to the same quality management and who use the same audit methodologies and tools. This pressure will also cause increased concentration of the audit market for both work on components for group audits as well as for the other work on components by auditors, such as statutory audits. These market effects are not in line with the policies set forth by the European Commission and national governments in the EU and could be viewed as being anti-competitive.

While the risk-based approach as proposed will improve the treatment of the financial information of components that are individually not significant, but are collectively significant, we are convinced that that risk-based approach as contemplated by the draft will result in inappropriate assessment of the risks of material misstatement of the group financial statements and the inappropriate design and performance of appropriate responses to those assessed risks for significant components. Furthermore, the way the draft is written, it will mislead group engagement teams into inappropriately seeking to perform, at component level, risk assessment procedures, identify and assess the risks of material misstatements, and design and perform further audit procedures, even though they are not capable of doing so effectively. We provide our reasoning in the treatment of the main issues below.

KSW

We are concerned that the risk-based approach to group audits may not result in appropriate risk assessments. It may even lead to more procedures on group level without improving audit quality.

It has implications for the extent of involvement of component auditors and there is a risk that some risks of material misstatement will be missed. The involvement of component auditors in the risk assessment process is vital as component auditors might be aware of local risks which are not known by the group engagement team. It would be helpful to emphasize the need for sufficient local knowledge that may be needed to better understand the entity and its operating environment and to avoid the risk that component auditors may focus on the assigned work rather than identifying and assessing risks at the component level.

5. Accounting Firms

NEXIA

United states 1

GERMANY

We would like to address our concerns re the proposed standard on group audit (ISA 600) which, together with ISA 220 revised, pursues a one engagement team concept and a top-down approach. The emphasis of this approach has significant impact on market concentration both under current and future regulations in the EC.

Under current law there are already a variety of constellations in which a so-called “shared audit with an auditor from another network is caused or at least encouraged by existing EU regulation. These include the following constellations in particular:

(1) PIE/CRR-PIE: Due to the different rotation periods, in practice (e.g. Siemens) the possibility is used to appoint another auditor after ten years only for the Financial Services Group.
(2) PIE outside EU/EU-PIE: In these cases, too, there is a need in practice to restrict the legally required change of auditor to the EU area (example Goldman Sachs).

(3) Non-PIE/CRR-PIE: Quite a few large SMEs are subject to EU requirements only with their banking activities. In this constellation, the fee limit for consulting services at the level of the parent company, which would otherwise have to be observed, often plays an additional role.

(4) Mandate constellations within the group due to different PIE definitions and rotation periods within the EU (including Belgium, Italy, Poland, Portugal) as well as appointment periods of several years may also require the use of several audit firms.

This enumeration of the cases of different auditors at the Group Auditor and Component Auditor level caused by EU regulation makes it clear that the public policy perspective on the ISA 600 standard is already of considerable importance on the basis of the current regulatory environment. In these mandate constellations, the auditor at component level does not necessarily come from the circle of small and medium-sized audit firms. In our view, the approach adopted by the IAASB (one engagement team concept, overemphasis on the top-down approach) is therefore counterproductive to the needs already existing in practice to deal with the existing EU regulation.

Furthermore, it is not unlikely that as a result of the audit reform on both sides of the Channel joint and/or audit will find greater application in future, both in the UK and the EC. The IAASB should therefore carefully reconsider whether the approach chosen in ISA 600 is not contradictory to other regulatory developments of significant importance.

It is hard to object to the principle that a group audit should be conducted using a risk-based approach. It should help to ensure that the group engagement team focuses its work effort appropriately on the riskier areas.

However, for our group audits, it seems inevitable that ED-600 will make the process longer, particularly in relation to the risk assessment, without changing the overall outcome in terms of risks identified and work done by the group engagement team and component auditors. This will have a negative effect on audit quality, as it is unlikely that the client will be prepared to pay for the extra time involved.

We have concerns that the revised definition of “component”, the focus on account balances, transactions and disclosures across the group, and the change in approach to using component auditors could lead to risks being missed in the risk assessment (for example in relation to related parties, fraud and non-compliance with laws and regulations at a local level) or local risks identified not being appropriately assessed. This is less likely to be the case under the current standard, which requires a minimum level of local risk assessment. It would be helpful to emphasise that, in making their risk assessment, the group engagement team must ensure that it is based on sufficient local knowledge.

JAPAN

The risk-based approach to the standard is consistent with the approach taken across other auditing standards. There must be acknowledgement from regulators, however, that in taking this approach different firms could potentially arrive at alternative audit approaches when considering the same group. In the UK specific guidance has been issued by the regulator (FRC) which made it clear the extent to which audit workpapers should be obtained and/or reviewed by group audit teams depending upon whether a component was considered to be significant or not significant. This led to a straightforward approach to evidence expected to be on files relating to component work. Additional clarity over this area was clearly required in respect of the existing ISA 600 in the UK and this could have been overcome however ED-600
does not provide such clarity. In practice this will be difficult to apply and, in our opinion, will lead to a divergence in practice in terms of whether component work is reviewed or not without additional guidance.

United Kingdom 1

United Kingdom 2

Use of significant component concept

- We think that it is extremely difficult for a group engagement team to complete risk evaluation procedures solely by themselves. A group engagement team needs involvement of component auditors who have more knowledge on the business environments of a component.

Therefore, the approach in current ISA 600 that a group engagement team identify significant components and use component auditors for the audit of the significant components is reasonable. By this approach, sufficient audit resources can be devoted in high-risk area.

7. Member Bodies and Other Professional Organizations

WPK

We very much support all efforts to improve audit quality in the public interest.

However, regarding the general approach taken in ED ISA 600, we do have the following severe concerns:

Asymmetry between centralized risk assessment (top-down-approach) and decentral risk assessment (bottom-up-approach)

According to ED-600.31, the group engagement team shall take responsibility for the identification and the assessment of all risks of material misstatement of the group financial statements (centralized risk assessment or top-down-approach).

When the group engagement team involves component auditors in the risk assessment procedures (as described in paragraph 25) or in the identification and assessment of the risks of material misstatement of the group financial statements, the group engagement team shall consider the results of the component auditors’ work (ED-600.32), i.e. the results of the risk assessment procedures performed by component auditors and in particular any risks identifies and assessed by them. Also, ED-600.25 states that when the group engagement team assigns the design and performance of risk assessment procedures to component auditors, the group engagement team shall consider the results of those procedures.

It is, however, left to the professional judgement of the group auditor, whether or not the group auditor assigns the design and performance of any risk assessment procedures to component auditors. In other words, the group auditor may decide to involve component auditors for risk assessment purposes, resulting in a combination of risk assessment procedures performed centrally (top-down approach) and risk assessment procedures performed decentrally (i.e. locally) by component auditors (bottom-up approach). However, similarly the group engagement team (i.e. the core group engagement team of the audit firm appointed as group auditor) may choose to perform a central risk assessment only without involvement of any risk assessment procedure by component auditors.

Under extant ISA 600 the performance of risk assessment procedure performed by local component auditors and the consideration of the results by the group engagement team, are enforced in a more reliable way. For example extant ISA 600 prescribes the performance of full scope audits for all components that are significant due to their individual financial significance to the group. This requirement guarantees a local,
decentralised risk assessment for all such components, regardless of whether these audits are performed by the group engagement team or a component auditor.

If those full scope audits are performed by component auditors, the group engagement team is required to be involved in the component auditor’s risk assessment. This includes, as a minimum, discussing with the component auditor the component’s business activities, and susceptibility of the component to material misstatement of the financial information due to fraud or error and reviewing the component auditor’s documentation of identified significant risks of the group financial statements (extant ISA 600.30). The same minimum requirement applies to any audits performed by component auditors for components that are significant to the group because they are likely to include group significant risks.

In theory, even extant ISA 600 allows the group engagement team to avoid the use of any component auditors by performing full scope audits for significant components by itself. In practice, however, in the case of geographically diverse groups, in particular international or global groups, the group engagement team has little choice but to use full scope audit-engagements performed by local auditors (either of the same network or not) for purposes of a group engagement team.

Potential negative consequences:

Whilst extant ISA 600 enforces a decentralised risk assessment (at least for all significant components), proposed ED-600 is characterised by a strong asymmetry by favouring a centralised risk assessment (top-down approach) as opposed to a decentralized, local risk assessment performed by component auditors (bottom-up approach). The extent to which local risk assessment is performed is left to the professional judgement of the group auditor. Proposed ED 600 would even allow group auditor to completely refrain from performing decentralised, local risk assessment procedures and to perform a single centralised risk assessment only.

We believe that such an approach is not convincing and counterintuitive given the increasing diversification and internationalization of groups that can be observed in recent years.

From our perspective, maintaining or even strengthening a decentralized risk assessment would be a more convincing way forward. The increasingly multipolar global economy strengthens the need to take advantage of a component auditor’s more granular understanding of the respective component and its business activities and his extended experience with the economic, legal and cultural environment, in which the respective competent operates.

Accordingly we suggest, that any future version of ISA 600 continues to require a minimum level of decentralised risk assessment activities performed by local component auditors (or the core group engagement team itself), in particular with regard to the larger components and any components affected by significant or heightened risks of material misstatement.

Abolishing the requirement to perform full scope audits at component level

Under extant ISA 600.26 the performance of a “full scope audit” was prescribed for all components of a group that are significant due to their individual financial significance to the group.

Proposed ED-600 does not require the identification of significant components, nor does it prescribe a minimum work effort or type of work to be performed for any component of a group, regardless of their size or nature.

Potential negative consequences:
In contrast to extant ISA 600, the proposed ED-600 allows the group engagement team to decide – based on its professional judgment – whether or not to perform a full scope audit at the component level. In practice the group engagement team may even decide to perform no full scope audit at all at the component level, even for the largest or most significant components of a group. Whilst under extant ISA 600 the reader of an ISA 600 group audit opinion could rely on the fact that all components of individual financial significance were subject to a full scope audit, under proposed ED-600 a similar insight is not available for the users of a group audit report. This reduces significantly the information of a (future) group audit opinion regarding the work effort and persuasiveness of the procedures performed for purpose of an ISA group audit.

In addition to this, there is a risk that the abolishment to perform a full scope audit at component level is likely to result in a „race to the bottom“ of audit quality in the context of group audit proposals. In particular in tender situations, when group management asks interested audit firms for providing an alternative, minimum scoping approach as part of their proposals, there is a risk that such alternative scoping approaches would fall significantly short of the current minimum group audit work effort (i.e. the requirement of a full scope audit to be performed for all individually significant components) in the interest of achieving a more competitive overall audit price.

Reducing or even abolishing the performance of full scope audits at component level also results in a risk that neither the group engagement team nor individual component auditors will have a comprehensive overview of the circumstances of individual (significant) components at the time the Group auditor's report is issued (see also section 3 of our comment letter).

In the interest of both audit quality and audit consistency we suggest that any future version of ISA 600 continues to require a minimum extent of full scope audits to be performed a component level, at least for the largest and most significant components of a group.

Changing the predominant type of work performed at component level from full scope audits into a combination of individual audit procedures for individual pieces of financial information

Extant ISA 600 clearly distinguishes four types of work to be performed at component level (extant ISA 600.27 and 29):

An audit of a financial information of a component (also called “full scope audit”),
An audit of one or more account balances, classes of transaction or disclosures,
A review of the financial information of the component,
Specified (audit) procedures.

By clearly distinguishing those four types of work, and by mandating the performance of full scope audits for significant components due to size, extant ISA 600 has established a group audit practice, where full scope audits performed at component level represent a predominant audit approach chosen by the group engagement team. In other words: full scope audits on the financial information of individual components, that are performed and completed before the group auditor’s report is issued, currently represent the backbone of audit evidence obtained for purposes of a group audit.

ED-600 proposes to abolish the obligation to perform full scope audits and to give up the systematic differentiation between different types of work to be performed at component level under extant ISA 600, where full scope audit plays the most prominent role. Instead, we believe that the new ED-600 promotes an
approach, where - with regard to the financial information of the individual component - the full scope audit will be replaced by a combination of the following activities (as the “usual” approach taken in practice):

For some selected pieces of the financial information of a component, the group engagement team will perform individual audit procedures centrally and at group level without the involvement of a component auditor (e.g. central audit for revenue transactions of the entire group, see ED-600 A64, A86),

For other selected parts of the financial information of a component, further audit procedures are performed locally / decentralised for individual components by a component auditor (or directly by the core group engagement team, i.e. without using a component auditor) (see ED-600 A87),

For some other parts of the financial information of a component, the group engagement team may choose to completely refrain from performing or instructing any further audit procedures.

Potential negative consequences:

We believe that one of the consequences of ED-600 will be that in many cases full scope audits currently performed for individual components would be replaced with a combination of some selected audit procedures as described above under a. - c. even in situations, where local statutory audits for components will continue to be mandated, we expect that component auditors would usually only perform audit procedures as described under b. before the date of the group auditor’s report. The remaining parts of the local statutory audits (i.e. full scope audits) can – and often will – be postponed to a later point of time, so that respective findings from that kind of work would not be available for purposes of a group audit.

Furthermore we believe that – everything else being equal – a mere combination of individual audit procedures as described under a. - c. and the resulting audit evidence would be less persuasive in comparison to a full scope audit performed at component level.

We also believe that replacing full scope audits with a combination of audit procedures as described under a. - c. means that neither the group engagement team nor individual component auditors will have a comprehensive overview and understanding of the circumstances of individual components at the time the group auditor’s report is issued. In particular in heterogeneous and multinational groups, we see a danger that - due to a less granular understanding of the circumstances at the level of individual components - relevant risks of material misstatements of a component that may be relevant to the group financial statements may not be identified.

Finally, we believe that the delineation of the extent of work that has to be performed by the component auditor for group audit purposes and the scope of his responsibilities will be less clear, if full scope audits are replaced by individual procedures as described under a. - c. The ISAs represent a clear framework for a component auditor’s responsibilities when conducting a full scope audit for purposes of a group audit. The ISAs, however, cannot be used as a framework or even reference point for what precisely a component auditor has to do, when he is instructed to perform some individual audit procedures only (be it individual risk assessment procedures, individual further audit procedures or a combination of both). Neither ISA 315 nor ISA 330 can be applied in isolation, since ISA 200, para18 and 20 mandates compliance with the entire set of relevant ISAs. Also, current practice under extant ISA 600 shows that specified audit procedures are often ill defined due to a lack of clarity in the respective audit instructions. ED 600, however, does not include any principles or guidance on how the description or delineation of specified audit procedures may be sufficiently improved or standardised to avoid misunderstandings between the group auditor and
components auditors regarding their respective responsibilities when instructing or performing specifies procedures.

Accordingly, we suggest that any future version of ISA 600 continues to distinguish different types of work that may be performed for the financial information of individual components. We also suggest that the performance of full scope audits for individual components should continue to play the most prominent role in that context.

Overreliance on a Centralized Fraud Risk Assessment at Group Level

We believe that abolishing the requirement to perform full scope audits at component level (see section 2 of our comment letter) and the general bias of ED-600 towards a centralised risk assessment (see section 1 of our comment letter) is particularly problematic with regard to the “Fraud Risk Assessment”.

According to extant ISA 600, the requirement to perform full scope audits at least for all components that are significant due to their individual size (extant ISA 600.26) and the requirement for the group engagement team to be involved in the risk assessment of all significant components (i.e. both due to size and due to risk) where component auditors perform an audit engagement, establishes and safeguards a decentralized fraud risk assessment. For example, in case of an international group, audits of significant components located in other countries than the parent entity are usually performed by (local) component auditors who have detailed knowledge of the local economic and legal conditions as well as of the cultural environment, including the respective local language. In contrast to the group engagement team, they are in a much better position to perform interviews regarding sensitive issues like fraud with local management and those charged with governance or of any other appropriate counterparts within the local component under audit. Also we believe that the nature of fraud risks and the degree to which they may affect different parts of financial information under audit may differ significantly from country to country, e.g. due to economic, legal or cultural differences. Thus, local component auditors are also in a better position to perform the procedures and risk assessment considerations required under ISA 240 when conducting a full scope audit or an audit of account balances for a particular component.

Finally, the requirement of extant ISA 600.30 for the group engagement team to be involved in the local risk assessment performed for all significant components ensures that the group engagement team is made aware of any fraud risks that component auditors may have identified locally.

We believe that it is not convincing to replace the bottom-up fraud risk assessment approach required under extant ISA 600 with a centralised fraud risk assessment approach. ED-600 introduces a fraud risk assessment approach where the group engagement team is only required to perform inquiries at the group level and where it is left to the judgement of the group engagement team whether or not to perform any related fraud risk assessment procedures at component level. And even if the (core) group engagement team decides to perform local risk assessment procedures for some selected components, it is again left to the judgement of the (core) group engagement team to decide whether or not to involve any component auditors with local knowledge when performing those procedures.

Potential negative consequences:

ED-600 results in an inappropriate overreliance on fraud risk assessment procedures performed at group level. We believe, that requiring fraud interviews to be conducted with group management and those charged with governance at group level only, whilst leaving it to the complete judgment of the group engagement team whether or not to perform fraud related inquiries with component management or component auditors (see ED-600 A80 last bullet point), neglects the existence of fraud risks at component
level and their relevance for the group financial statements in particular in the case of a diversified, large and international group.

The reliability and the persuasiveness of the fraud risk assessment performed at the component level will be significantly reduced by scaling back or even abolishing the involvement of local component auditors in performing fraud risk assessment procedures. Similarly, replacing the entire fraud risk assessment under ISA 240 - that represents an integral and iterative part of a full scope audit performed for a component - by some individually specified risk assessment procedures also reduces the chance of identifying fraud risks that reside a component level.

ED-600 neglects the importance of local legal and cultural peculiarities of fraud risks. We believe, it is almost ineffective, if a member of a (core) group engagement team conducts a fraud interview with component management in another country without sharing the same native language and without an appropriate understanding of relevant economic, legal and cultural differences.

Strengthening the group audit principles of extant ISA 600 - a missed opportunity!

Extant ISA 600 became effective more than 10 years ago. Over that period of time, the standard has established a number of generally accepted group audit principles, which are well known in the global audit profession and even by many audit clients. Examples of these group audit principles are the identification of significant components (extant ISA 600.12 and 18a), the requirement to perform full scope audit-engagements for components that are significant due to their size (extant ISA 600.26), and a prescribed minimum involvement of a group engagement team in the work performed by component auditors (extant ISA 600.30 and 31) and a clear distinction of four different types of work to be performed at component level (extant ISA 600.27 and 29). Instead of abolishing all these principles – as foreseen by ED-600 – we suggest maintaining and further strengthening these established group audit principles as follows:

ISA 315 (Rev. 2019) will have to be implemented in 2 years time. The introduction of the spectrum of inherent risks and inherent risk factors will lead to more standardized and granular way of identifying, assessing and documenting risks of material misstatement. We believe that once those principles are implemented for audits performed for individual components, a group engagement team applying extant ISA 600 will be in a significantly better position to be involved in the risk assessment of component auditors (e.g. in case of significant components) or to request component auditors to report relevant results of their risk assessment to the group engagement team in a standardised way (e.g. in case of non-significant components). We believe that ISA 315 (Rev. 2019) offers the opportunity to result in a significantly improved communication between the group engagement team and component auditors about their results of the risk assessment. This opportunity has not yet been sufficiently explored and ought to be discussed in more depth by adding respective application guidance to the involvement requirements of extant ISA 600.

One of the backbones of extant ISA 600 is the identification of "group significant risks". Group significant risks are important for the current group audit approach in two ways: Firstly, they result in the identification of components that are significant due to risk (extant ISA 600 A6). Secondly, they result in involvement requirements regarding the further audit procedures performed in response to those significant risks by component auditors (extant ISA 600.31).

Again, we believe that the issuance of ISA 315 (Rev. 2019) provides an opportunity to significantly improve the quality of group audits performed under extant ISA 600. ISA 315 (Rev. 2019) introduces a new definition for the term “significant risk” and aligns that definition with the concept of the spectrum of inherent risks and the application of inherent risk factors. Implementing this new definition of the term "significant risk" for purposes of identifying group significant risks provides the group engagement team with the opportunity of a
more robust and consistent identification of these group significant risks. This can be further strengthened, for example, by requesting component auditors to report any kind of significant risks identified locally (including those for local statutory audits) to the group engagement team, thus providing it with a more holistic overview of which significant risks exist across all components of a group. Again, we suggest that extant ISA 600 should be strengthened by adding application guidance on the identification of group significant risks based on the new principles of ISA 315 (Rev. 2019).

The above considerations also apply to accounting estimates and related disclosures in the context of a group audit. The implementation of ISA 540 (Rev.) by the global audit profession, which is currently taking place, provides group engagement teams with the opportunity of identifying risks associated with accounting estimates on a group wide basis in a much more consistent way. Again, we believe that ISA 540 (Rev.) provides the opportunity to develop guidance to complement extant ISA 600 on auditing accounting estimates in a group audit. E.g. the group engagement team could request component auditors to report back their findings and assessments with regard to methods, assumptions and data for any accounting estimates identified at component level in a standardised way. This will also improve the group engagement team’s ability to identify accounting estimates that are associated with group significant risks.

Extant ISA 600.42 (b) includes a relatively weak review requirement regard the component auditor’s documentation. Currently, it is a complete judgment call of the group engagement team to decide whether or not to perform such a work paper review (“the group engagement team shall determine whether it is necessary to review other relevant parts of the component auditor’s audit documentation”). Instead of completely redefining the term “group engagement team” (by including the component auditors) as proposed in ED-600/ED-220, it would be a much easier and straightforward approach to strengthen the review requirement of extant ISA 600.42, e.g. by introducing and specifying a minimum extent of working paper reviews to be performed when using the work of component auditors. We believe that adding a requirement and respective application guidance on which parts of the documentation for audits of significant and non-significant components need to be reviewed by the group engagement team will result in an immediate and effective improvement of both the overall involvement of the group engagement team and the group audit quality.

We strongly urge the IAASB to examine all possibilities for sharpening and reemphasizing the existing requirements of extant ISA 600 and supplementing the respective application materials to pursue the opportunities of improving group audit quality as described above. This is of particular importance with regard to the potential audit quality improvement triggered by implementing ISA 315 (Rev. 2019) and ISA 540 (Rev.) in the context of a group audit.

Lack of consideration of the practical implications of ISA 540 (Rev.) and ISA 315 (Rev. 2019) in the context of a group audit

As discussed above (see section 1 of our comment letter) ED-600 foresees a centralised risk assessment performed by the group engagement teams (top-down approach). By the time ISA 600 becomes effective (we presume at the earliest in 2 or 3 years), the risk assessment performed in an ISA-Audit will significantly change as a result of implementing ISA 540 (Rev.) and ISA 315 (Rev. 2019). We believe that ED-600 does not yet contemplate or discuss in a sufficient way the practical implications which ISA 540 (Rev.) and ISA 315 (Rev. 2019) will have in the context of a group audit, in particular for the co-operation of a (core) group engagement team with the component auditors.

Examples of major practical changes to the risk assessment triggered by ISA 540 (Rev.) and ISA 315 (Rev. 2019) include:
The introduction of the concept of a spectrum of inherent risk,

The application of inherent risk factors,

A new definition and a new approach for identifying significant risks,

A more standardised and granular risk assessment for accounting estimates, including the explicit consideration of methods, assumptions and data.

Whilst it remains to be seen how the audit profession changes its risk assessment practices over the next two years, we believe that the following developments can already now be observed:

Several international audit networks will change their way of assessing their inherent risks from a two level system (e.g. inherent risks are either significant or non-significant) to a system distinguishing three or even more levels (e.g. low, moderate, significant).

More audit firms will distinguish different types of potential misstatements/root causes as a basis for their risk assessment, as opposed to an assertion-based or an assertion-focused risk assessment.

Firm-specific audit manuals will foresee more differentiated audit responses (i.e. further audit procedures) in response to the more granular risks of material misstatement.

We believe that the centralisation of such a more granular and detailed risk assessment at the group level poses a much larger challenge for audit firms than anticipated by ED-600. Also, it would go significantly beyond the challenge of centralising the current risk assessment practice (i.e. risk assessment performed for ISA-Audits until the busy season 2019/2020).

Potential negative consequences:

In the case of large, diversified groups, there is a risk that the centralisation of the assessment and documentation of all risk of material misstatement identified throughout the group will become too confusing or even impractical. In other words, we believe that a group engagement team that documents (or at least tries to document) all risks identified throughout a large, diversified group "can't see the forest for the trees".

It is to be expected that the more granular risk assessment introduced by ISA 315 (Revised 2019) and ISA 540 (Revised) will result in more differentiated guidelines (e.g. audit manuals) on suitable responses to those risks, which makes a centralised planning and documentation of those responses of the respective further audit procedures even more complicated.

The Group Audit Instructions, which will have to include both information regarding the more granular risk and the more granular further audit procedures, will need to be further expanded and become potentially confusing.

The competition-distorting disadvantages of non-network-related component auditors will increase even further (ED-600 A83, see section 5 of our comment letter).

Lack of a Framework regarding the Intensity of the Involvement at Component Level

Extant ISA 600 (Para 30 and 31) clearly defines a minimum involvement of the group engagement team regarding:

the risk assessment of significant components where an audit is to be performed and further audit procedures in response to significant risk performed at component level.
Extant ISA 600 also prescribes the depth of that involvement (see ISA 600.30 a-c and 31 sentence 1 and 2), including for example discussing with the competent auditor the component's business activities and the susceptibility of the component to material misstatement due to fraud or error, reviewing the component auditors documentation of significant risks and evaluating the appropriateness of the further audit procedures to be performed to respond to those significant risks.

Proposed ED-600.23 foresees that the group engagement partner – when planning the direction and supervision the component auditors and the review of their work – “takes into account” areas of higher assessed risk of material misstatement (including significant risks) and areas in the group financial statements that involve significant judgment. Also, ED-600 A50 includes some qualitative considerations on how the direction, supervision and review of the component auditor's work may be tailored, however, without describing any hard thresholds or conditions for a minimum involvement into the work of the component auditor.

We believe that neither the scope nor the depth of the involvement of the group engagement partner is clearly defined under ED-600 and remains highly judgmental.

Potential negative consequences:

The term “takes into account” areas of higher assessed risk or areas that involve significant judgment does not provide a clear minimum threshold for the involvement into the work of the component auditor. Accordingly, the focus of the group engagement partner’s or team’s attention will be very judgmental, even more so in case of a heterogeneous group with a large number of international components. We believe it is unhelpful to say “takes into account” without explaining “how” to take this into account, e.g. by highlighting the principles that drive that consideration.

The lack of minimum requirements regarding the involvement in the work performed at component level will result in a greater inconsistency of the involvement approaches applied by different audit firms or networks, again in particular with regard to complex international groups. This will also reduce the ability of users of future group audits, including audit committees or any readers of group audit reports, to evaluate the effectiveness and persuasiveness of group audit engagements.

Q8 – No Comment

2. Investors and Analysts
CRUF
No Comment

4. National Auditing Standard Setters
AUASB
No comment

ICAI
No Comment
5. Accounting Firms
CR
No comment
ETY
No comment
MAZUSA
No comment
MNP
No comment

6. Public Sector Organizations
AGA
No comment
AGC
No comment
AGM
No comment

7. Member Bodies and Other Professional Organizations
BICA
No comment
CalCPA
No comment
CAQ
No Comment
ECA
No comment
IBRACON
No comment

ICPAS
No comment

IIA
No comment

IMCP
No comment

INCP
No comment

NYSSCPA
No comment

8. Academics
AFAANZ
No comment

GRAHAM
No Comment

HUNTER
No comment

LI
No Comment

9. Individuals and Others
PITT
No Comment

VERA
No comment