

Engagement Team – Group Audits Independence (Clean)

INTERNATIONAL INDEPENDENCE STANDARDS (PARTS 4A AND 4B)

PART 4A – INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS

SECTION 400

APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS

Introduction

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- 400.1 It is in the public interest and required by the Code that professional accountants in public practice be independent when performing audit or review engagements.
- 400.2 This Part applies to both audit and review engagements. The terms “audit,” “audit team,” “audit engagement,” “audit client,” and “audit report” apply equally to review, review team, review engagement, review client, and review engagement report.
- 400.3 This Part applies to all members of the audit engagement team, including an individual from a component auditor firm who performs audit work related to a component for purposes of a group audit. Section 405 sets out specific independence provisions applicable in a group audit.

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Note: Paragraph numbers 400.A – 400.D below are placeholders and will be renumbered once the provisions have been finalized and included in Section 400. All paragraphs in Section 400 that follow these new provisions will be renumbered accordingly.

Engagement Team and Audit Team

- 400.A An engagement team for an audit of financial statements includes all partners and staff in the firm who perform audit procedures on the engagement, and any other individuals who perform such procedures who are from:
- (a) A network firm; or
 - (b) A firm that is not a network firm, or another service provider.
- For example, an individual from a component auditor firm who performs audit work on the financial information of a component in a group audit is a member of the engagement team for the group audit.
- 400.B In ISQM 1, a service provider includes an individual or organization external to the firm that provides a resource that is used in the performance of engagements. Service providers exclude the firm, a network firm or other structures or organizations in the network.

- 400.C An audit engagement might involve experts from the firm or a network firm, external experts or, in the case of a group audit, experts from a component auditor firm outside the group auditor firm's network, who assist in the engagement. Depending on the role of the individuals, they might be members of the engagement team or the audit team. For example:
- Individuals with expertise in a specialized area of accounting or auditing who perform audit procedures are members of the engagement team. These include, for example, individuals with expertise in accounting for income taxes or in auditing client information using automated tools and techniques.
 - Individuals within or engaged by the firm who have direct influence over the outcome of the audit engagement through consultation regarding technical or industry-specific issues, transactions or events for the engagement are not members of the engagement team but are audit team members.
 - Individuals who are external experts in fields other than accounting or auditing are not members of the engagement team or the audit team.
- 400.D If the audit engagement is subject to an engagement quality review, the engagement quality reviewer and any other individuals performing the engagement quality review are not members of the engagement team but are audit team members.

SECTION 405

GROUP AUDITS

Introduction

- 405.1 Section 400 requires a firm to be independent when performing an audit engagement, including a group audit engagement, and to apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence. This section sets out specific requirements and application material relevant to applying the conceptual framework when performing group audit engagements.

Requirements and Application Material

General

- 405.2 A1 The ISAs apply to an audit of group financial statements. This section addresses the relevant independence considerations that apply in a group audit. ISA 600 (Revised) deals with special considerations that apply to an audit of group financial statements, including when component auditors are involved. ISA 600 (Revised) requires the group engagement partner to confirm whether the component auditors understand and will comply with the relevant ethical requirements, including those related to independence, that apply to the group audit. The independence requirements referred to in ISA 600 (Revised), or other relevant auditing standards applicable to group audits that are equivalent to ISA 600 (Revised), are those specified in this section.
- 405.2 A2 A component auditor firm that participates in a group audit engagement might separately issue an audit opinion on the financial statements of the component. Depending on the circumstances, the component auditor firm might need to comply with different independence requirements when performing procedures for a group audit and separately issuing an audit opinion on the financial statements of the component for statutory, regulatory or other reasons.

Independence Considerations Applicable to Individuals

- R405.3** All audit team members for the group audit shall be independent of the group audit client in accordance with the requirements of this Part that are applicable to the audit team.

Independence Considerations Applicable to a Group Auditor Firm

- R405.4** A group auditor firm shall be independent of the group audit client in accordance with the requirements of this Part that are applicable to the firm.

Independence Considerations Applicable to Network Firms of a Group Auditor Firm

- R405.5** A network firm of the group auditor firm shall be independent of the group audit client in accordance with the requirements of this Part that are applicable to the network firm.

Independence Considerations Applicable to Component Auditor Firms outside a Group Auditor Firm's Network

All Group Audit Clients

- R405.6** A component auditor firm outside the group auditor firm's network:
- (a)** Shall be independent of the component audit client in accordance with the requirements set out in this Part that are applicable to a firm with respect to all audit clients; and
 - (b)** Shall not hold a direct or material indirect financial interest in the entity on whose group

financial statements the group auditor firm expresses an opinion.

R405.7 Consistent with paragraph R400.20, when a component auditor firm outside the group auditor firm's network knows, or has reason to believe, that a relationship or circumstance involving any related entity of the component audit client other than related entities over which the component audit client has direct or indirect control is relevant to the evaluation of the component auditor firm's independence from the component audit client, the component auditor firm shall include that related entity when identifying, evaluating and addressing threats to independence.

R405.8 When a component auditor firm outside the group auditor firm's network knows, or has reason to believe, that interests or relationships of a firm within the component auditor firm's network with the component audit client or the group audit client create a threat to the component auditor firm's independence, the component auditor firm shall evaluate and address any such threat.

Group Audit Clients that are Public Interest Entities

R405.9 When the group audit client is a public interest entity, a component auditor firm outside the group auditor firm's network shall be independent of the component audit client in accordance with the requirements set out in Part 4A that apply to a firm with respect to public interest entities.

Key Audit Partner

405.10 A1 The group engagement partner might determine that the engagement partner on the audit of a component is a key audit partner for the group audit because that individual makes key decisions or judgments on significant matters with respect to the group audit. In these circumstances, once the group engagement partner has communicated that determination to the engagement partner on the audit of the component, that individual will be subject to the provisions in paragraphs R411.4 and R524.6 and Section 540 that apply to key audit partners.

Proposed consequential amendment to definition of Key Audit Partner

The engagement partner, the individual responsible for the engagement quality review, and other audit partners, if any, on the engagement team who make key decisions or judgments on significant matters with respect to the audit of the financial statements on which the firm will express an opinion. Depending upon the circumstances and the role of the individuals on the audit, "other audit partners" might include, for example, engagement partners for the audits of certain components in a group audit such as significant subsidiaries or divisions.

Non-Assurance Services

405.11 A1 Section 600 requires a firm to evaluate whether non-assurance services provided to an audit client create threats to independence. The application of paragraph R405.9 requires a component auditor firm to apply the independence requirements for non-assurance services for public interest entities to the component audit client where the group audit client is a public interest entity. For example, where the group audit client is a public interest entity, the component auditor firm is prohibited from acting in an advocacy role for a component audit client that is not a public interest entity in resolving a dispute or litigation before a tribunal or court, regardless of whether the amounts involved are material to the financial information of the component audit client. Similarly, the component auditor firm's design and implementation of the component audit client's financial information system that generates the financial information on which the component auditor firm will perform audit work would create a self-

review threat and would therefore be prohibited if the group audit client is a public interest entity.

- 405.11 A2 The financial information on which a component auditor firm performs audit work is relevant to the evaluation of the self-review threat that might be created from the component auditor firm's provision of a non-assurance service. For example, if the component auditor firm is only performing audit work on a specific item such as inventory, the evaluation of the self-review threat would only include non-assurance services that form part of or affect the accounting records or the financial information related to the accounting for, or the internal controls over, inventory.

Changes in Component Auditor Firms

All Group Audit Clients

- 405.12 A1 There might be circumstances in which the group auditor firm requests another firm to perform audit work as a component auditor firm during or after the period covered by the group financial statements. A threat to the component auditor firm's independence might be created by:
- (a) Financial or business relationships of the component auditor firm with the component audit client during or after the period covered by the group financial statements but before the component auditor firm agrees to perform the audit work; or
 - (b) Previous services provided to the component audit client by the component auditor firm.
- 405.12 A2 Paragraphs 400.31 A1-A3¹ set out application material that is also applicable for a component auditor firm's assessment of threats to independence if a non-assurance service was provided by the component auditor firm to the component audit client during or after the period covered by the group financial statements, but before the component auditor firm begins to perform the audit work for the purposes of the group audit, and the service would not be permitted during the engagement period.

Breach of an Independence Provision by a Component Auditor Firm

When a Component Auditor Firm Within the Group Auditor Firm's Network Identifies a Breach

- R405.13** If a component auditor firm within the group auditor firm's network identifies a breach, the component auditor firm shall communicate the breach immediately to the group auditor firm. Based on the assessment of the component auditor firm's breach, the group auditor firm shall determine what action to take in accordance with the provisions of paragraphs R400.80 to R400.89.

When a Component Auditor Firm Outside the Group Auditor Firm's Network Identifies a Breach

- R405.14** If a component auditor firm concludes that a breach of a relevant ethical requirement applicable to the group audit has occurred, the component auditor firm shall:
- (a) End, suspend or eliminate the interest or relationship that created the breach and address the consequences of the breach;
 - (b) Evaluate the significance of the breach and its impact on the component auditor firm's objectivity and ability to perform audit work for the purposes of the group audit; (Ref: Para 400.80 A2)

¹ Note to IESBA: The numbering for paragraphs 400.31 A1-A3 will be updated when the revised NAS provisions become effective.

- (c) Depending on the significance of the breach, determine whether it is possible to take action that satisfactorily addresses the consequences of the breach and whether such action can be taken and is appropriate in the circumstances; and (Ref: Para 400.80 A3)
- (d) Promptly communicate the breach to the group engagement partner, including the component auditor firm's assessment of the significance of the breach and any actions proposed or taken to address the consequences of the breach.

R405.15 Upon receipt of the component auditor firm's communication of the breach, the group engagement partner shall:

- (a) Review the component auditor firm's assessment of the significance of the breach and any actions proposed or taken to address the consequences of the breach;
- (b) Evaluate the impact of the breach on the component auditor firm's objectivity and the group auditor firm's ability to use the work of the component auditor firm for purposes of the group audit; and
- (c) Determine the need for any further action.

R405.16 In making this determination, the group engagement partner shall exercise professional judgment and take into account whether a reasonable and informed third party would be likely to conclude that the component auditor firm's objectivity is compromised, and therefore, the group auditor firm is unable to use the work of the component auditor firm for the purposes of the group audit.

405.17 A1 If the group engagement partner determines that the breach has been satisfactorily addressed by the component auditor firm and does not compromise the component auditor firm's objectivity, the group auditor firm may continue to use the work of the component auditor firm for the group audit.

405.17 A2 In certain circumstances, the group auditor firm might determine additional actions are needed to satisfactorily address the breach in order to use the component auditor firm's work. Examples of such action include the group auditor firm performing specific procedures on the areas impacted by the breach or requesting the component auditor firm to perform appropriate remedial work on the affected areas.

405.17 A3 If the breach cannot be satisfactorily addressed, the group auditor firm cannot use the component auditor firm's work. In those circumstances, the group auditor firm might decide to find other means to obtain the necessary audit evidence on the component audit client's financial information. Examples of such means include the group auditor firm performing the necessary audit work on the component audit client's financial information or requesting another component auditor firm to perform such audit work.

Communication with Those Charged with Governance of the Group Audit Client

R405.18 When a component auditor firm outside the group auditor firm's network identifies that a breach of the relevant ethical requirements relevant to the group audit has occurred, the group auditor firm shall discuss with those charged with governance:

- (a) The significance of the breach at the component auditor firm, including its nature and duration; and
- (b) Whether actions proposed or taken would satisfactorily address the consequences of the breach and the impact on the component auditor firm's objectivity in order to enable the group auditor firm to use the work of the component auditor firm.

Such discussion shall take place as soon as possible unless an alternative timing is specified

by those charged with governance for reporting less significant breaches.

R405.19

If those charged with governance do not concur that the actions proposed or taken satisfactorily address the consequences of the breach at the component auditor firm, the group auditor firm shall not use the work performed by the component auditor firm for the purposes of the group audit, unless additional actions can be taken in order to obtain the concurrence of those charged with governance.

GLOSSARY, INCLUDING LISTS OF ABBREVIATIONS

Defined Terms Relating to Proposed Section 405

(Clean)

Audit team for the group audit	<p>(a) The engagement team for the group audit, including individuals from component auditor firms who perform audit work related to components for purposes of the group audit;</p> <p>(b) All others within or engaged by the group auditor firm who can directly influence the outcome of the group audit, including:</p> <p>(i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the group engagement partner in connection with the performance of the group audit, including those at all successively senior levels above the group engagement partner through to the individual who is the firm's Senior or Managing Partner (Chief Executive or equivalent);</p> <p>(ii) Those who provide consultation regarding technical or industry-specific issues, transactions or events for the group audit; and</p> <p>(iii) Those who perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the group audit; and</p> <p>(c) All those within a network firm who can directly influence the outcome of the group audit.</p>
Component	An entity, business unit, function or business activity, or some combination thereof, determined by the group auditor for purposes of planning and performing audit procedures in a group audit
Component audit client	<ul style="list-style-type: none">• When a component is a legal entity, the entity and any related entities over which the entity has direct or indirect control.• When a component is a business unit, function or business activity (or some combination thereof), the legal entity or entities to which the business unit belongs or in which the function or business activity is being performed.
Component auditor firm	The firm performing audit work related to a component for purposes of the group audit
Group audit	The audit of group financial statements
Group audit client	The entity on whose group financial statements the group auditor firm conducts an audit engagement. The group audit client includes its related entities as specified in paragraph R400.20 and any other components that are subject to audit work.

Group auditor firm	The firm that expresses the opinion on the group financial statements
Group engagement partner	The engagement partner who is responsible for the group audit
Group financial statements	Financial statements that include the financial information of more than one entity or business unit through a consolidation process

GLOSSARY, INCLUDING LISTS OF ABBREVIATIONS

Proposed Revised Definitions of Engagement Team, Audit Team, Assurance Team and Review Team

(Clean)

- Assurance Team
- (a) All members of the engagement team for the assurance engagement;
 - (b) All others within the firm, or engaged by the firm, who can directly influence the outcome of the assurance engagement, including:
 - (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the assurance engagement partner in connection with the performance of the assurance engagement;
 - (ii) Those who provide consultation regarding technical or industry specific issues, transactions or events for the assurance engagement; and
 - (iii) Those who perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the engagement.

- Audit Team
- (a) All members of the engagement team for the audit engagement;
 - (b) All others within the firm, or engaged by the firm, who can directly influence the outcome of the audit engagement, including:
 - (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the engagement partner in connection with the performance of the audit engagement, including those at all successively senior levels above the engagement partner through to the individual who is the firm's Senior or Managing Partner (Chief Executive or equivalent);
 - (ii) Those who provide consultation regarding technical or industry-specific issues, transactions or events for the engagement; and
 - (iii) Those who perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the engagement; and
 - (c) All those within a network firm who can directly influence the outcome of the audit engagement.

In Part 4A, the term "audit team" applies equally to "review team."

- Review Team
- (a) All members of the engagement team for the review engagement; and
 - (b) All others within the firm, or engaged by the firm, who can directly influence the outcome of the review engagement, including:
 - (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the engagement partner in connection with the performance of the review engagement, including those at all successively senior levels above the engagement partner through to the individual who is the firm's Senior or Managing Partner

(Chief Executive or equivalent);

- (ii) Those who provide consultation regarding technical or industry specific issues, transactions or events for the engagement; and
 - (iii) Those who perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the engagement; and
- (c) All those within a network firm who can directly influence the outcome of the review engagement.

Engagement
team

All partners and staff performing the engagement, and any other individuals who perform procedures on the engagement, excluding an external expert and internal auditors who provide direct assistance on the engagement.

In Part 4A, the term “engagement team” refers to individuals performing audit or review procedures on the audit or review engagement, respectively.

(ISA 220 (Revised) provides further guidance on the definition of engagement team in the context of an audit of financial statements.

ISA 620 deals with the auditor’s responsibilities relating to the work of an individual or organization in a field of expertise other than accounting or auditing, when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence.

ISA 610 (Revised 2013) deals with the auditor’s responsibilities if using the work of internal auditors, including using internal auditors to provide direct assistance on the audit engagement.)

In Part 4B, the term “engagement team” refers to individuals performing assurance procedures on the assurance engagement.

Note to IESBA

The Task Force is also proposing the following conforming amendments to Section 360 to align with terminology in the proposed ISA 600 (Revised).

PART 3 - PROFESSIONAL ACCOUNTANTS IN PUBLIC PRACTICE

SECTION 360

RESPONDING TO NON-COMPLIANCE WITH LAWS AND REGULATIONS

Communication with Respect to Groups

- R360.16** Where a professional accountant is performing work on the financial information related to a component for the purposes of a group audit and becomes aware of non-compliance or suspected non-compliance in relation to the component, the accountant shall communicate the matter to the group engagement partner unless prohibited from doing so by law or regulation. The communication to the group engagement partner shall be in addition to responding to the matter in accordance with the provisions of this section.
- R360.17** Where a professional accountant is performing an audit of the financial statements of an entity or a business unit for purposes other than a group audit, for example, a statutory audit, and becomes aware of non-compliance or suspected non-compliance in relation to the entity or business unit of the group, the accountant shall communicate the matter to the group engagement partner unless prohibited from doing so by law or regulation. The communication to the group engagement partner shall be in addition to responding to the matter in accordance with the provisions of this section.
- 360.18 A1 The purpose of the communication in paragraphs R360.16 and R360.17 is to enable a group engagement partner to be informed about the matter and to determine, in the context of the group audit, whether and, if so, how to address it in accordance with the provisions in this section.
- R360.19** Where the group engagement partner becomes aware of non-compliance or suspected non-compliance in the course of an audit of group financial statements, the group engagement partner shall consider whether the matter might be relevant to one or more components whose financial information is subject to work for purposes of the audit of the group financial statements. If so, the group engagement partner shall take steps to have the matter communicated to those performing work at the components, unless prohibited from doing so by law or regulation. This consideration shall be in addition to responding to the matter in the context of the group audit in accordance with the provisions of this section.
- R360.20** Where the group engagement partner becomes aware of non-compliance or suspected non-compliance in the course of an audit of group financial statements, the group engagement partner shall consider whether the matter might be relevant to entities or business units whose financial statements are subject to audit for purposes other than the group audit, for example, a statutory audit. This consideration shall be in addition to responding to the matter in the context of the group audit in accordance with the provisions of this section.
- R360.21** If the non-compliance or suspected non-compliance might be relevant to one or more of the entities or business units specified in paragraph R360.20, the group engagement partner shall take steps to have the matter communicated to those performing work at the entities or business units, unless prohibited from doing so by law or regulation. If necessary, the group engagement partner shall arrange for appropriate inquiries to be made (either of management

or from publicly available information) as to whether the relevant entity(ies) or business unit(s) specified in paragraph R360.20 is subject to audit and, if so, to ascertain to the extent practicable the identity of the auditor.

- 360.22 A1 The purpose of the communication in paragraphs R360.19 and R360.21 is to enable those responsible for work at the components, entities or business units to be informed about the matter and to determine whether and, if so, how to address it in accordance with the provisions in this section.