

May 16, 2016

## **IFAC Small and Medium Practices Committee Response to the IAASB's Invitation to Comment, *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits***

### **INTRODUCTION**

The SMP Committee (SMPC) is pleased to respond to the IAASB (the Board) on this Invitation to Comment (ITC). The SMPC is charged with identifying and representing the needs of its constituents and, where applicable, to give consideration to relevant issues pertaining to small-and medium-sized entities (SMEs). The constituents of the SMPC are small-and medium-sized practices (SMPs) who provide accounting, assurance and business advisory services principally, but not exclusively, to clients who are SMEs. Members and Technical Advisers serving the SMPC are drawn from IFAC member bodies representing 22 countries from all regions of the world.

### **GENERAL COMMENTS**

The SMPC has closely followed the development of the ITC and submitted comment letters in advance of a number of the IAASB quarterly Board meetings on each of the respective topics. We support the IAASB in considering quality control, professional skepticism and group audits at this time.

The ITC is an excellent and well-written document. In particular, we appreciate the inclusion of paragraphs covering the SMP perspective throughout the ITC and welcome the approach taken to outline the issues, the references to existing requirements and application material, followed by the possible actions to address the issues.

As outlined in the comment letter we submitted to the IAASB in September 2015, we are, however, concerned that the length of the ITC will not encourage responses from many SMPs. In our view, three shorter documents covering the projects individually would have been more manageable and better suited to obtaining feedback. To the extent that there are cross-over issues these could have been mentioned in each shorter paper. In addition, the title is enhancing audit quality, whereas the scope of ISQC 1<sup>1</sup> covers firms' responsibilities for quality control beyond audit services. Many SMPs do not provide audit services and may therefore not respond to the ITC even though some of the proposals may directly affect them.

We strongly believe that the Board needs to give more consideration to using less conventional ways of eliciting feedback and comments on its proposals, in order to obtain input from the largest possible number of SMPs. Due to their often limited resources, SMPs are not able to easily respond and engage with the standard setting consultation process. This demands actively seeking out their views, rather than waiting

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<sup>1</sup> International Standard on Quality Control (ISQC 1), *Quality Control for Firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Services Engagements*



for them to respond to often complex and long exposure drafts and consultation papers. One proposal is to work closer with IFAC member organizations to organize specific initiatives to obtain feedback from SMPs.

The IAASB should also recognize the risk of non-response bias with the likely absence of SMP responses as it analyzes the comment letters to the ITC and considers the actions for each project. This is an area in which it may be helpful to obtain the assistance of academics, who could assist in the analysis and run some generally accepted tests for evidence of such bias, as well as advising on ways to minimize nonresponse bias in the future.

We are concerned that there is a potential for these projects to lengthen the suite of ISAs considerably, since the majority of actions raised involve additional clarifications or strengthening of requirements. The SMPC believes that the IAASB must be sensitive to balancing the burden arising from changes to standards and the likely benefits to the public interest. Keeping up with new regulations and standards has been consistently ranked as one of the top challenges facing SMPs in the Global SMP Surveys conducted by IFAC<sup>2</sup>. The costs and burden of the adoption of revised standards is felt more acutely by SMPs, who may not have the necessary in-house resources to easily implement revisions. We strongly believe that piecemeal changes to the requirements in isolated standards should be avoided wherever possible and that there is a robust and rigorous cost/ benefit analysis of the potential impact on both SMPs and SMEs in the Board's consideration of future changes in each project.

In particular, the projects could also result in enhanced documentation requirements. This continues to be an area of concern for many SMPs. The IAASB needs to consider that the perception of many regulators that "if it is not documented, it is not done" against the need to ensure documentation concentrates on significant matters and judgments encountered in the audit rather than becoming excessive. An excessive focus on documentation and a tick-box mentality in general can even be detrimental to audit quality, especially if they serve to take valuable time and resources resulting in less professional judgment being exercised.

In addition, as many of the calls for action in the ITC seem to reflect inappropriate or non-application of the current standards, the SMPC is not convinced that revision is the most appropriate way of dealing with all the issues. We encourage the IAASB to consider other initiatives to assist with the practical application of the ISAs, such as Staff FAQs (frequently asked questions), illustrative examples and enhanced dialogue with regulators regarding the efficacy of standard-setting to deal with non-compliance issues.

The SMPC supports the IAASB considering the QMA approach as this would be better suited to allowing firms to tailor quality control measures to their individual specific circumstances. We have consistently stated that certain aspects of ISQC 1 are perceived as imposing a disproportionate burden on smaller practices. We therefore support the IAASB's focus on scalability and a broader approach to enable firms to consider quality management in the context of all types of engagements. In particular, a proactive management of engagement quality that encourages individual engagement team members to fulfill their

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<sup>2</sup> IFAC Global SMP Survey Results 2015: (see <http://www.ifac.org/publications-resources/ifac-global-smp-survey-2015-results>)



respective roles will be more effective to optimizing quality than an exercise purely reviewing past performance. We believe that the consideration of the needs of SMPs should be central to this aspect of the project.

The Board should ensure that the costs of implementing a QMA approach do not disproportionately impact SMPs. In particular, the smallest firms who make up the majority of firms in public practice. For example, sole practitioners represented 39% of the 6,725 respondents to the latest IFAC SMP Global Survey with 32% from firms with only 2-5 partners and staff. ISQC 1 impacts most services commonly performed by all SMPs. However, the IAASB needs to be very sensitive to the SMP/SME environment as some SMPs may be less involved in certain sectors of the audit market compared to larger firms, but many SMPs continue to perform audits of financial statements. In certain jurisdictions audits of fairly small entities may be required by law, but in some jurisdictions, especially those which have introduced thresholds for statutory audits, SMPs may also perform a significant number of voluntary audits. Overall, we agree with the revision of ISQC 1, but recognize that SMPs may require a lot of support to help them make the transition to the QMA.

The SMP Committee does not consider that ISA 600<sup>3</sup> is fundamentally broken, but recognizes there are a number of issues and that have led to inconsistencies in practice, which should be addressed to improve the quality of group audits. We note that many of the issues identified are logistical and may not be resolved from standard setting alone.

It is important that the revision of ISA 600 does not have any unintended consequences on audit quality by negatively impacting SMPs through inappropriate changes to the standard resulting in SMPs being accepted less as component auditors, or precluded from assuming the role of group auditor. Whilst we support many of the proposed actions that will be explored, it is essential for the IAASB to be able to distinguish between gaps in the standard (where additional requirements may be needed) and incorrect application of the standard (where potentially further explanation or training may be appropriate), so as not to over-engineer its suite of standards, nor to result in an excessive focus on documentation so as to address the concerns of regulators' or audit oversight bodies at the expense of the SMP auditor community.

## **SPECIFIC COMMENTS**

We have outlined our responses to the questions (in bold italics) in the ITC below.

### **General**

***G1. Table 1 describes what we believe are the most relevant public interest issues that should be addressed in the context of our projects on professional skepticism, quality control, and group audits. In that context:***

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<sup>3</sup> ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*



- (a) Are these public interest issues relevant to our work on these topics?***
- (b) Are there other public interest issues relevant to these topics? If so, please describe them and how, in your view, they relate to the specific issues identified.***
- (c) Are there actions you think others need to take, in addition to those by the IAASB, to address the public interest issues identified in your previous answers? If so, what are they and please identify who you think should act.***

The public interest issues identified are relevant to the work on the topics.

The SMP Committee supports the inclusion of encouraging proactive quality management at the firm and engagement level and believes it is in the public interest to consider what can be done to encourage a scalable and robust approach to quality that is fostered by proactive firm leadership and management.

We consider that ‘fostering an appropriately independent and challenging skeptical mindset of the auditor’ is very important. We see this as closely linked to Continuing Professional Development (CPD), which often focuses more on technical matters, such as changes to laws and regulations. The “soft skills” of professional skepticism and “tone at the top” are more questions of mind and attitude. These skills lend themselves more towards practical case studies and exercises, rather than lessons transmitting pure information.

Training in the application of professional skepticism is difficult for firms of all sizes but particularly for SMPs. We believe that professional organizations that provide training, and commercial training providers should create more CPD opportunities specifically related to professional skepticism. In addition, there may be more limited opportunities for mentoring in some SMPs and therefore Professional Accountancy Organizations (PAOs) could facilitate some kind of mentoring as a substitute for small firms and sole practitioners.

An additional public interest issue relevant to these topics is data analytics. The SMP Committee IAASB Rapid Response Task Force (IRRTF) recently had the opportunity to discuss this with the relevant IAASB Working Group and it is clear that it presents both opportunities and challenges for SMPs. The ICAEW publication [Data Analytics for External Auditors](#) acknowledges that software solutions are becoming increasingly available in the SMP market in a number of jurisdictions and it is likely that the use of data analytics will become more common going forward.

Pressure to lower fees has been consistency ranked as one of the top challenges facing SMPs in the IFAC Global SMP Surveys and we believe should also be a matter addressed by the Joint Working Group. There is concern that lower fees may result in lower audit quality and greater difficulties for firms to pay competitive salaries in order to attract talented individuals. These factors, combined with higher responsibility and questions being asked about the prestige of auditors, may make it difficult to attract and retain the top talent



as auditors. Quality audits are in the public interest and all stakeholders (e.g. regulators, investors, governments and businesses) need to coordinate to ensure that the right incentives are there for auditors to deliver quality, including having sufficient time and adequate resources. At present, for a variety of good reasons, the incentives sometimes do not align.

***G2. To assist with the development of future work plans, are there other actions (not specific to the topics of professional skepticism, quality control, and group audits) that you believe should be taken into account? If yes, what are they and how should they be prioritized?***

From the list of most relevant public interest issues, we believe that ‘keeping ISAs fit for purpose’ should be of high importance for the IAASB going forward. As acknowledged in the ITC, the IAASB standards must be capable of being applied to audits of all types of entities globally. Therefore the standards need to remain principles based such that they can provide latitude for professional accountants to adapt to changes in the environment and so the ISAs are also perceived as remaining fit for purpose going forward.

The SMPC recognizes that the IAASB needs to be responsive to a broad cross section of stakeholders many with diverging views, interests and priorities. We acknowledge that the regulators and those representing listed entities and PIEs, some highly complex and specialized, may be pressing for the standards to be tailored to their specific needs. It is likely, however, that these needs may not be compatible with those of SMEs and SMPs and those other stakeholders may have more resources to advocate for particular changes.

The SMP Committee is committed to facilitating the implementation of international standards. It developed the [Guide to Using International Standards on Auditing in the Audits of Small- and Medium-Sized Entities](#) in 2007, which has been downloaded over 90,000 times, has 28 translations completed or in progress and is used for firms in training and as a practical tool. The Guide is in its third edition and will be updated in 2016 to reflect changes to the standards since the last edition in 2011. The Committee also conducts numerous [outreach activities](#) including presentations on how to apply the ISAs efficiently for audits of SMEs and giving visibility to the IAASB staff publication to explain how the ISAs can be applied to audits on a proportional basis<sup>4</sup>.

In our view, the consultation on the [Nordic Standard for Audits of Small Entities \(SASE\) in October 2015](#) by the Nordic Federation of Public Accountants (NRF) highlighted certain concerns about the implementation of the ISAs, in particular for SMPs and audits of micro entities. We understand that the consultation received over 200 responses from a wide range of stakeholders, including IFAC member organizations and national auditing standard setters, not just in the Nordic region.

We recognize that the dialogue and liaison with the NRF is ongoing. However, we believe that the project raises important issues that may warrant further consideration by the Board. For example, there may be

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<sup>4</sup> [Applying ISAs Proportionately with the Size and Complexity of an Entity](#), IAASB Staff Publication, 2009



initiatives that the IAASB could consider and prioritize as part of its work plan in 2017 – 2018, as well as in its future strategy 2020 – 2024. This could include undertaking a further information gathering exercise, for instance with the National Standard Setters (NSS), in order to fully understand the issues and concerns raised about the use of the ISAs for smaller entities. The Board may also need to undertake more systematic and timely post implementation reviews of its standards as the last review of the clarified ISAs was completed in 2013.

In addition, we believe that the matter may need to be considered from a long-term perspective in order to find a meaningful solution and ensure that the ISAs are fit for purpose for audits for all sizes and complexity.

***G3. Are you aware of any published, planned or ongoing academic research studies that may be relevant to the three topics discussed in this consultation? If so, please provide us with relevant details.***

We are not aware of any relevant academic studies on the three topics, but fully support the IAASB in asking this question and its willingness to consider academic research as part of the ITC.

### **Professional Skepticism**

The application of appropriate professional skepticism is fundamental to the conduct of a quality audit. In the SMPC [response](#) to the *IAASB Proposed Strategy for 2015-2019 and Proposed Work Program for 2015-2016* we raised concerns about the amount of resources that could be allocated to this project and which may outweigh the potential benefits and any resulting change in auditor behavior, as it cannot be addressed through standard setting alone.

The call for action is partly based on the reported globally recurring theme in inspection findings that auditors did not sufficiently apply professional skepticism in their audits. We therefore support the IAASB seeking to understand the “root causes” of these inspection findings and the extent to which they do indicate a lack of professional skepticism.

***PS1. Is your interpretation of the concept of professional skepticism consistent with how it is defined and referred to in the ISAs? If not, how could the concept be better described?***

Our interpretation of professional skepticism is consistent with the definition in ISA 200<sup>5</sup>.

***PS2. What do you believe are the drivers for, and impediments to, the appropriate application of professional skepticism? What role should we take to enhance those drivers and address those impediments? How should we prioritize the areas discussed in paragraph 37?***

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<sup>5</sup> ISA 200, *Overall Objectives of the Independent Auditor, and the Conduct of an Audit in Accordance with International Standards on Auditing*



The drivers for, and impediments to, professional skepticism include the culture within a firm, especially the “tone at the top” and its approach to training and educating staff. As identified in the ITC, time and resource constraints may also be significant inhibitors to an auditors’ application of professional skepticism, as well as individual personality traits and local norms and cultures in certain jurisdictions. In addition, it is important that partner’s allocate adequate time to each engagement and ensure that the audit team has sufficient guidance on the application of professional skepticism throughout the engagement.

We are aware that there are trends towards shorter reporting deadlines and in some jurisdictions the issue of audit reports is concentrated in a few months of the year (so-called “busy season”). The pressure for the audit team to complete the work in a short period of time is very high and, particularly where a client supplies key accounting information at a late stage in the audit (e.g. on an accounting estimate) it is increasingly difficult to ensure that the audit staff and partners have sufficient time to apply professional judgment and demonstrate professional skepticism efficiently and effectively.

We welcome the Joint Working Group which has been established to consider professional skepticism by the IAASB, IESBA and IAESB to make recommendations to each standard setting board whether there is standard-setting or related work that can be undertaken. We believe that coordination on this issue is extremely important and any action the Board decides to take should be aligned with the treatment of these matters by the other boards.

In our view, out of the areas being explored, the IAASB should prioritize whether there is a consistent and accurate understanding amongst auditors of what is meant by “professional skepticism”, if the concept is consistently described across the ISAs, IESs, and IESBA Code and whether the current requirements and guidance in the International Standards are clear as to what is expected from auditors. In addition, the IAASB should consider the potential effect of the evolving use of technology on professional skepticism in audits as part of its project on data analytics. This is likely to be an increasingly important issue, especially as audits are more likely to be undertaken “offsite” utilizing technology. There is a risk that auditors may be less skeptical using data from technology.

We believe the IAASB needs to thoroughly explore the notion of professional skepticism. If having done so, the Board decides to develop a professional skepticism framework or professional judgment framework it is important to avoid this being a “checklist procedure”. While some guidelines may help the auditor, there is a risk it may encourage the wrong behavior that following such “framework instructions” is a guarantee of professional skepticism and correct work.

***PS3. Is the listing of areas being explored in paragraph 38–40 complete? If not, what other areas should we or the Joint Working Group consider and why? What do you think are the most important area to be considered?***

In our opinion, the list of areas being explored seems complete. We consider that the IAASB efforts related to quality control are the most important. In particular, how firm leadership and accountability, firm culture



and strategy, as well as actions by the engagement partner can better promote the application of professional skepticism.

We believe that it would be helpful if through the Joint Working Group there could be some clarification between professional skepticism and the relevant concepts in the IESBA Code of independence in mind and due care.

***PS4. Do you believe the possible actions we might take in the context of our current projects relating to quality control and group audits will be effective in promoting improved application of professional skepticism? If not, why?***

Whilst we support the Board exploring opportunities to reinforce the concept of professional skepticism as part of its current projects, there is a risk that including specific requirements for professional skepticism throughout individual ISAs may give the impression it is only needed in certain areas or more so than in other places. We believe the Board should focus on how the application material can provide more guidance on ways to exercise and demonstrate professional skepticism. This is particularly important in those areas where the auditor's judgment is required to be applied. For example, in areas of accounting with high estimation uncertainty this may include considering a number of different scenarios and documenting why management's decision is appropriate.

***PS5. What actions should others take to address the factors that inhibit the application of professional skepticism and the actions needed to mitigate them (e.g., the IAESB, the IESBA, other international standards setters or NSS, those charged with governance (including audit committee members), firms, or professional accountancy organizations)? Are there activities already completed or underway of which we and the Joint Working Group should be aware?***

We are not aware of any other activities which are completed or underway of which the IAASB and Joint Working Group should be aware. However, we suggest that the Joint Working Group also considers the matter of fortitude (i.e. the strength of mind that enables the auditor to deal with matters arising during the course of the audit with courage) identified in the ITC.

We consider that the Staff Questions & Answers – *Professional Skepticism in an Audit of Financial Statements*<sup>6</sup> is a useful tool in providing guidance. The Board should work with NSS and PAOs to promote this existing guidance and increase the chances that those that need to read it will do so.

The recent IAESB Consultation Paper: *Meeting Future Expectations of Professional Competence: A Consultation on the IAESB's Future Strategy and Priorities* included particular actions to improve professional competence related to the appropriate exercise of professional skepticism and professional judgment. The SMP Committee's [response](#) stated that the development of practical tools, such as short on-line video case studies, may assist member organizations with fewer resources for use in their training

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<sup>6</sup> <http://www.ifac.org/publications-resources/staff-questions-answers-professional-skepticism-audit-financial-statements>



materials. In our opinion, both concepts can be difficult to understand, especially for students, and material with examples and guidance on how to effectively exercise professional judgment and skepticism may be useful. We also acknowledged that standard setting boards may not be the appropriate parties to produce such practical tools.

## **Quality Control**

***QC1. We support a broader revision of ISQC 1 to include the use of a QMA as described in paragraphs 45–67.***

***(a) Would use of a QMA help to improve audit quality? If not, why not? What challenges might there be in restructuring ISQC 1 to facilitate this approach?***

The SMP Committee considers that the use of a QMA approach could significantly help to improve audit quality. It should help firms design and implement effective quality management systems that take into account the size and nature of the firm, the services it provides and the nature of its client base.

In our view quality should be managed and continuously improved – it is not static. A quality management approach should be integrated in the culture and values of a firm. It could be argued that whilst ISQC 1 provides a minimum quality level, it does not consider how to improve quality. A QMA embraces an attitude to improve quality across the whole organization.

In theory, there is potential for simplification for many SMPs compared to the rigid approach under the extant version of ISQC 1. However, we are concerned about the potential for a QMA to add a burden on SMPs, not least as it will involve changes from extant application of ISQC 1 and believe the IAASB needs to be sensitive to how it can be applied in practice, in particular for firms with only a few partners. The Board will need to consider how the QMA approach should be scalable, such that it can be applied by a wide range of firms, from SMP firms with no audit engagements to large firms with listed entity clients. There may also be a need for tools or guidance on how to apply a QMA for small practices in the future, together with awareness raising and training.

A significant challenge for the Board in restructuring ISQC 1 to facilitate this approach is the considerable amount of rewriting that will need to take place and the resources involved.

***(b) If ISQC 1 is restructured to require the firm’s use of a QMA, in light of the objective of a QMA and the possible elements described in paragraphs 64 and Table 3, are there other elements that should be included? If so, what are they?***

In our opinion, the elements of a QMA described are complete. In monitoring quality there is reference to improvement, but we recommend this is emphasized to encourage a constant attitude to improving quality.



***(c) In your view, how might a change to restructure ISQC 1 impact the ISAs, including those addressing quality control at the engagement level?***

We agree that the restructure of ISQC will impact ISA 220<sup>7</sup> as indicated.

It is unclear which of the existing ISQC 1 requirements may no longer apply to SMPs. We note that the ITC states revising ISQC 1 to incorporate the use of a QMA may provide the Board with the opportunity to provide guidance as to how firms might consider whether and how corporate governance principles may be helpful or relevant. For SMPs such supplementary material and guidance is even more important as such principles will not have been designed specifically with smaller entities in mind.

In addition, the Board needs to ensure that the costs of implementing a QMA approach does not disproportionately impact SMPs. In particular, for the smallest firms who make up the majority of firms in public practice. For example, sole practitioners (39%) and firms with 2-5 partners and staff (32%) represented 71% of respondents to the latest IFAC SMP Global Survey.

For QMA to be most effective it needs to be embraced by individual team members as staff at all levels have a responsibility to fulfill their respective roles to optimize quality.

***(d) If ISQC 1 is not restructured to require the firm's use of a QMA, do you believe that we should otherwise address the matters described in paragraph 59 and table 2, and if so, how?***

If ISQC 1 is not restructured to require the firm's use of a QMA it should be reviewed to be adapted to SMPs as it currently has a "one size fits all" approach.

We support the consideration of a QMA and agree with an enhanced focus in ISQC 1 on the importance of, and need for, effective firm leadership as a foundation to the ability of the firm to achieve quality.

***QC2. Engagement Partner Roles and Responsibilities***

***(a) Paragraphs 69–86 set out matters relating to the roles and responsibilities of the engagement partner.***

- (i) Which of the actions outlined in paragraphs 85–86 would be most meaningful to address issues related to engagement partner responsibilities?***
- (ii) Why do you believe these actions are necessary?***

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<sup>7</sup> ISA 220, *Quality Control for an Audit of Financial Statements*



- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Describe any potential consequences of possible actions that you believe we need to consider further.**

In our opinion, the proposal to add an appendix to ISA 220 that indicates where the responsibilities of the engagement are articulated within the requirements and application in the ISAs would be helpful.

The SMP Committee generally agrees with many of the actions to address the issues, but considers some of these tend to be more relevant to medium and large practices rather than SMPs. We encourage the Board to carefully consider the impact of the possible actions on the smallest firms. For example, we fully agree on the importance of the engagement partner in creating a quality climate to lead staff, but depending on the final wording used this aspect may be considered primarily applicable to large firms. The issue seems to us to revolve around the need for engagement partners to “embrace” quality in all their actions, since depending on individual circumstances, engagement partners contribute to engagement quality in their own right as well as “by-example”.

**(b) Do you think it is necessary for the ISAs to include requirements or otherwise address the circumstances described in paragraph 79 in which an individual other than the engagement partner is required to or otherwise customarily sign(s) the auditor’s report or is named therein? If yes, please explain why, and provide your views about how this could be done (including describing the work effort you believe would be necessary for such an individual).**

As the signature of an audit report can be stipulated in country law or regulation, the IAASB may be unable to be too prescriptive with the ISAs containing requirements dealing with the responsibilities of an individual being named in or signing the auditor’s report when such individual is not the engagement partner. However, we support further exploration on the extent of the issue as we believe that it would be inappropriate for an individual to sign the auditor’s report without at a minimum performing the same procedures that an engagement quality control reviewer (EQCR) would perform, since a signatory is seen to accept a certain responsibility for the audit.

### **QC3. Others Involved in the Audit**

**(a) Paragraphs 87–104 set out matters relating to involvement of others in the audit:**

- (i) Which of the actions outlined in paragraphs 100–104 would be most meaningful to address issues related to others participating in the audit?**
- (ii) Why do you believe these actions are necessary?**



- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Describe any potential consequences of possible actions that you believe we need to consider further.**

In our opinion, as many of the issues raised are based on concerns expressed by regulators and seem to reflect unsuitable or non-application of the extant ISAs, the IAASB should also consider clarification or guidance rather than a revision of the relevant requirements.

We are concerned that making reference to the report of another auditor in the auditor's report undermines the auditor's overall responsibility for the audit. In addition, we do not consider that information on an auditor's expert is appropriate in the auditor's report, but support making such information available to management and those charged with governance. We believe that information included in the auditor's report should not detract from the communication that it is the engagement partner who takes overall responsibility for an audit engagement.

**(b) Should we develop further requirements or application material for circumstances when other auditors are involved in an audit engagement (i.e., auditors that don't meet the definition of component auditors)?**

We support the Board considering clarification of the role of the engagement partner in situations where other auditors (other than component auditors) are involved in the audit.

#### **QC4. The Firms' Role in Supporting Quality**

**(a) Paragraphs 106–123 set out matters relating to networks of firms and use of ADMs.**

- (i) Which of the actions outlined in paragraphs 114–116 and 122–123 would be most meaningful to address issues related to firms operating as part of a network of firms and firms' changing business models and structures?**
- (ii) Why do you believe these actions are necessary?**
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Describe any potential consequences of possible actions that you believe we need to consider further.**



***(b) Specifically:***

***(i) What could we do to address the issues identified in the context of networks of firms? For example, should we develop more detailed requirements and application material to address reliance on network-level policies and procedures at a firm or engagement level?***

***(ii) Do you think it would be feasible for us to develop requirements and guidance for networks? Please provide a basis for your views.***

***(iii) Paragraphs 117–123 set out matters relating to the use of ADMs and related issues.***

***a. How should our standards emphasize the importance of appropriate quality control processes in relation to use of ADMs?***

***b. Are you aware of ADMs that raise issues not discussed in paragraphs? If so, please provide details.***

We agree that it will be challenging for the Board to develop requirements for networks because of the reasons outlined. In addition, the SMPC is aware that the borders between networks, associations and alliances are increasingly blurred. In practice differences between some organizations self-defined as networks and others that qualify themselves in different ways are not always very clear when analyzing their real structure and performance. For example, even the less formal organizations have in common some training (or regular conferences) and some kind of quality control, to be sure that when referring someone, quality is appropriate. The use of common brands, disclosure terms etc. can also be very similar in networks and associations and it is clear that an association can be a network even if it calls itself otherwise.

The SMP Committee agrees that individual firms need to be able to support and document their reliance on network quality control policies and monitoring procedures. As there are a number of different ways in which these may be organized, and because of the differences in laws and regulations in jurisdictions, a flexible and principles-based approach is needed by the IAASB.

On occasion the SMP-auditor may be excluded from the role of component auditor if the group auditor perceives that they can more easily deal with a component auditor who is part of the group auditor's network. However, this may not always be the case. For example, the increased benefit to audit quality resulting from common policies of a network firm (about which the group auditor would also need to be satisfied were working effectively) may be outweighed by a variety of other factors, such as industry know-how of a non-network firm or familiarity with cultural aspects that the network firm lacks. For this reason, the SMPC considers it important that where networks span jurisdictions, all factors listed in paragraph 242(c) be taken into account together, and not individually. The factors listed have a collective impact on the selection of component auditor and the nature and extent to which the group auditor needs to be involved in the work of component auditors.



**QC5. Governance of the Firm, Including Leadership Responsibilities for Quality**

**(a) Paragraphs 125–135 set out matters relating to governance of firms, including leadership responsibilities for quality.**

- (i) Which of the possible actions outlined in paragraphs 131–135 would be most meaningful in addressing issues related to firm governance and leadership responsibility for quality?**
- (ii) Why do you believe these actions are necessary?**
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.**

**(b) Specifically:**

- (i) Do you believe it is necessary for us to explore how the governance of a firm could be addressed in ISQC 1?**
- (ii) Should ISQC 1 specifically address accountability of firm leadership, or appropriate personnel within firm leadership, for matters related to quality, including independence related matters? If so, how should this be done, and what direction should ISQC 1 provide to firms in appointing appropriate individuals to assume these responsibilities?**
- (iii) Would the use by firms of a QMA provide better support or context for the importance of quality-related responsibilities for firm leadership, and related accountability, and therefore better facilitate the ability of firms to address these matters?**

We agree that firm leadership has a vital role in establishing and monitoring policies and procedures to achieve quality-related objectives and promoting a culture for accountability for quality throughout the firm. However, as noted in our response to QC1(c) we encourage the Board to be sensitive to the needs of firms of all sizes (including the smallest) and develop standards which are scalable to their individual circumstances and environment.

We agree that establishing a requirement in ISQC 1 for firm leadership to act in the public interest would be challenging to design and implement and do not believe it would be appropriate. In our opinion, the lack of a clear definition and common understanding of public interest remains an issue. The interpretation of acting in the public interest would likely prove highly subjective. In addition, there may be varying degrees of public interest inherent in the engagements performed by firms. However, we strongly suggest that the IAASB publicly and prominently acknowledge the public interest in the contribution of SMEs, including SMPs, to the global economy. This, of itself, is reason to ensure that the changes proposed are scalable.



The proposal to only include an emphasis on the importance of public interest considerations in relation to the design of the firm's system of quality control in the introduction to ISQC 1 or in the application material is supported.

**QC6. Engagement Quality Control Reviews and Engagement Quality Control Reviewers**

**(a) Paragraphs 136–146 set out matters relating to engagement quality control reviews and engagement quality control reviewers.**

- (i) Which of the possible actions outlined in paragraphs 143–146 would be most meaningful in addressing issues related to EQC reviews and EQC reviewers?**
- (ii) Why do you believe these actions are necessary?**
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.**

**(b) Specifically:**

- (i) Should ISQC 1 mandate the performance of EQC reviews beyond audits of listed entities? If yes, what other entities should be considered and how could we best define these entities? If no, please explain your reasoning.**
- (ii) Do you believe it is necessary for ISQC 1 to require that firms define the minimum period of time between when an individual has been the engagement partner and when that individual would be eligible to serve as the EQC reviewer on the same engagement? If yes, how do you think this should be done and why? If no, please explain why.**
- (iii) Would you support the development of a separate EQC review standard? Please explain the reasoning for your response.**

The SMP Committee agrees that the EQC Review is a key aspect in firms having effective systems of quality control. We support the IAASB exploring the issues identified in paragraphs 137-139 in the ITC.

We agree that SMPs face particular challenges with the often limited availability of individuals able to take on the role of an EQC reviewer. We are therefore concerned about the possible expansion of engagements that would require an EQCR beyond audits of listed entities and do not support this proposal.

In many jurisdictions PIEs include quite small entities, which are often audited by SMPs. We are therefore concerned that the proposals may disproportionately affect SMPs, without necessarily enhancing the



quality of the audit, and as a result impact the market concentration and could ultimately force some SMPs out of the PIE audit market, which may also impact audit quality and would not be in the public interest.

As recognized in the ITC, setting a minimum global definition or describing characteristics of entities of particular public interest other than listed entities that would be required to taken into account in setting a criteria for EQC reviews could be very difficult. The definition of a PIE varies from country to country and an entity may be a PIE because of the nature of its operations, its size or the number of its employees. The Board may wish to review the Federation of European Accountants (FEE) survey *Definition of Public Interest Entities (PIEs) in Europe*<sup>8</sup> which although published in 2015, still gives an impression of the wide diversity of definitions of PIEs applicable across European Countries. We also encourage the Board to consider the number of PIEs which are currently audited by SMPs worldwide, so as to obtain an understanding of the number of firms that could potentially find some of the current proposals problematic. A suggestion for consideration could be harmonizing with the public accountability concept used by the IASB in the IFRS for SMEs<sup>9</sup>.

On balance we do not support the possible action of developing a separate EQC Review standard. From an SMP perspective a separate standard might seem sensible, in particular for those firms who specifically do not take on work involving the type of risks an EQCR is intended to address. We also understand the objective to give greater prominence to the contribution of the EQCR to audit quality. However, since the EQCR was conceived as an internal firm check, we believe this could be achieved through revisions to ISQC 1 and consider it would give too much prominence to the role of the EQCR in comparison to the role of the engagement partner. Indeed, clarification of their respective roles may be helpful since the engagement partner has primary responsibility for the quality of the audit, whereas the EQC-reviewer may contribute to quality, but does not necessarily do so.

### **QC7. Monitoring and Remediation**

**(a) Paragraphs 147–159 set out matters relating to monitoring and remediation.**

- (i) Which of the possible actions outlined in paragraphs 156–159 would be most meaningful in addressing issues related to monitoring and remediation?**
- (ii) Why do you believe these actions are necessary?**
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.**

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<sup>8</sup> [http://www.fee.be/images/publications/auditing/PIE\\_definition\\_survey\\_outcome\\_141015.pdf](http://www.fee.be/images/publications/auditing/PIE_definition_survey_outcome_141015.pdf)

<sup>9</sup> See <http://www.ifrs.org/IFRS-for-SMEs/Pages/IFRS-for-SMEs.aspx>



***(b) Specifically:***

- (i) Do you support the incorporation of a new requirement(s) in ISQC 1 for firms to understand the causal factors of audit deficiencies relating to inspection findings and other reviews? If not, why? Are there any potential consequences or other challenges of taking this action that you believe we need to consider?***
- (ii) Do you support the incorporation of a new requirement(s) in ISQC 1 for the results of the firm's monitoring of the effectiveness and appropriateness of the remedial actions to be considered in the design and assessment of the effectiveness of the firm's***

We agree with the challenges identified for SMPs in monitoring and remediation. In our view, it would be helpful if some of the matters outlined could be addressed in the IAASB standards through application material. We also consider that IFAC PAOs and national standard setters have a role in providing practical guidance. Whilst we appreciate the desire to introduce requirements for understanding the causal factors of audit deficiencies, the Board must be sensitive to the challenges of SMPs and therefore any requirements should be capable of being applied proportionally and in enhancing the quality of the firm's audit engagement.

The IAASB may also consider the scope of the engagements included within the monitoring requirements in ISQC 1. For example, the inspection of a "completed engagement" (para. 48) and the extent to which this would be necessary for other assurance and related service engagements, and how this might be scalable according to the type of engagement.

***QC8. Engagement Partner Performance and Rewards Systems***

***Paragraphs 160–170 set out matters relating to engagement partner performance and rewards systems.***

- (a) Do you believe that establishing a link between compensation and quality in ISQC 1 would enhance audit quality? Why or why not?***
- (b) What actions (if any) do you believe we should take in this regard? Are there potential consequences of possible actions that you believe we need to consider?***

As noted in the ITC, from an SMP perspective the inclusion of a requirement that a component of an audit partner's remuneration be linked to incentives related to achieving audit quality may be challenging to implement and could have unintended consequences.

The SMP Committee is also not convinced that it is appropriate, or within the IAASB's mandate, to set standards to require that elements of a partner's remuneration should be variable and include incentives or disincentives linked to whether audit quality has been achieved. However, in practice, leading firms, small



and large do in fact incentivize audit quality and penalize its absence including through promotion and remuneration structures. Guidance to follow such practice would be helpful.

**QC9. Human Resources and Engagement Partner Competency**

**(a) Paragraphs 171–187 set out matters relating to human resources and engagement partner competency.**

- (i) Which of the possible actions outlined in paragraphs 176–178 and 187 would be most meaningful in addressing issues relating to human resources and engagement partner competency?**
- (ii) Why do you believe these actions are necessary?**
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.**

**(b) Specifically, which of the possible actions outlined, or other actions not described, in paragraphs 176–178 and 187 would most positively impact audit quality:**

- (i) Arising from issues related to knowledge, skills, competence and availability of a firm’s partners and staff?**
- (ii) Related to engagement partner competency?**
- (iii) Why do you believe these actions are necessary? If you would not support a particular action, please explain why, including any potential consequences of those actions that you believe we need to consider.**

Talent recruitment and retention are key challenges facing the profession. For example, the [AICPA Top Issues Survey](#) in 2015 found that talent pool concerns had emerged as the most pressing issue for all but the smallest CPA firms. The SMP Committee agrees that HR management is essential to achieving audit quality. We are also concerned about the potential knock-on effect on the pool of talent available to SMPs resulting from the [predicted significant fall in graduate recruitment](#) at some of the biggest auditors in some jurisdictions.

Based on the difficulties highlighted by SMPs in undertaking performance of staff reviews, the proposal to include additional application material that performance evaluations may be based on the facts and circumstances of the firm could be helpful, especially if it emphasizes continual feedback. We are concerned with the possibility of highlighting the importance of maintaining evidence of the procedures performed to address the requirements for a firm to have sufficient personnel with appropriate competence, capabilities and commitment to ethical principles. We agree that effective personnel management is a key



factor determining the quality of a firm's services. However, a rigid requirement to document processes may not work in an SMP environment, since the relatively limited number of staff available often means no "formal process" exists. The standard will need to be sufficiently flexible, to prevent documentation requirements simply becoming an end in themselves.

We would support a more detailed review of the relationship between IES 8 (Revised) and ISQC 1 and ISA 220. In our opinion, highlighting the competencies in IES 8 (Revised) in the areas of interpersonal and communication skills, professional skills and professional values, ethics and attitudes could be difficult.

### **QC10. Transparency Reporting**

**Paragraphs 188–190 set out matters relating to transparency reporting.**

- (a) Do you believe we are able to positively contribute to the evolving developments related to transparency reporting? If so, what, in your view, would be the most appropriate action we could take at this time?**
  
- (b) If you would not support us taking actions as described in paragraph 190(b), please explain why, including any potential consequences of those actions that you believe we need to consider.**

Currently transparency reporting is required in certain jurisdictions, and is generally confined to larger firms. The SMP Committee believes that requiring transparency reporting as an element of a firm's system of quality control would be beyond the IAASB mandate and it is only appropriate for regulators and audit oversight bodies to establish any requirements in this area. In our view, a requirement would likely impose burdens on SMPs that outweigh the public benefit. Moreover, it could widen the public perception of differences between larger and smaller firms if the IAASB standards were to require some firms to publish transparency reports and others not.

We support the Board facilitating ongoing dialogue on the topic and encouraging academic research. For example, we understand that in certain jurisdictions many firms actually submit very similar transparency reports each year.

**The following questions are overall questions relating to quality control:**

**QC11. Are there any other issues relating to quality control that we have not identified? If yes, please provide details. What actions should we take to address these issues?**

We do not have any other issues relating to quality control that have not been identified.

**QC12. Are there any other specific actions that others could take in relation to quality control? If yes, please provide details.**



The SMP Committee considers that stakeholders (including, regulators and supervisors) also have a key role to play in the perception of audit quality as their actions can directly impact the prestige and perception of the function, role and professionalism of auditors. For example, we recognize the important role of inspection findings reports, but are also aware how such findings can be widely and often reported, which may lead to some in society questioning the quality and ultimately also the value of audits. We believe that all stakeholders have a role in promoting the value of an audit and alleviating fee pressure, as well as explaining the responsibility for financial reporting (especially in financial scandals) of each party in the financial reporting supply chain. It is important that measures are taken to promote the positive image of an audit as more than just a commodity and obligation. This is necessary to assist with the pressure to lower fees (cheaper is not always better), as well as addressing issues with attracting and retaining top talent, which in-turn impacts audit quality.

***QC13. Are there any specific considerations for SMPs related to the issues and potential actions described in this section? Are there any other considerations for SMPs of which we should be aware? If so, please provide details and views about these matters.***

The public interest in the work performed by the profession is not uniform. While there is a widespread recognition of the collective contribution of SMEs to the global economy, and hence the sector's high level of public interest (which makes the scalability of ISAs critical), the public interest inherent in any one SMP's client base is typically much less than that of a large listed company. Similarly the composition of audit teams and degree of engagement partner involvement may vary considerably due to a number of factors, including the size of the firm.

We believe that the IAASB should remain sensitive to the need for its standards to be fully capable of proportionate application in all audit situations. When developing or modifying its standards, the IAASB should not look to add requirements, which are perhaps only justified for the more regulated "higher end" of the audit market, but less relevant or practical in smaller engagements and must ensure that any new requirements are either conditional, or where not, are capable of scalable application.

We appreciate that a QMA may benefit SMPs in the long-term as it may allow for flexibility in the application of policies and procedures based on the nature and extent of a firm's current and future activities and follows a risk-based approach. However, we also recognize that some aspects of the required changes will have cost implications. To the extent that larger firms may have already moved in this direction, the IAASB needs to be sensitive to the potential for changes to have a disproportionate impact on SMPs.

***QC14. Are there any specific public sector considerations related to the issues and potential actions described in this section? Are there any other public sector considerations of which we should be aware? If so, please provide details and views about these matters.***

We have no comments on public sector considerations.



## Group Audits

**GA1. We plan to revise ISA 600 (and other standards as appropriate) to respond to issues with group audits.**

***(a) Should we increase the emphasis in ISA 600 on the need to apply all relevant ISAs in an audit of group financial statements? Will doing so help to achieve the flexibility that is needed to allow for ISA 600 to be more broadly applied and in a wide range of circumstances (see paragraphs 194–198)? If not, please explain why. What else could we do to address the issues set out in this consultation?***

***(b) Would the actions we are exploring in relation to ISA 600 improve the quality of group audits? If not, why?***

***(c) Should we further explore making reference to another auditor in an auditor's report? If yes, how does this impact the auditor's work effort?***

***(d) What else could the IAASB do to address the issues highlighted or other issues of which you are aware? Why do these actions need priority attention?***

We agree that it may be helpful to increase the emphasis in ISA 600 on the need to apply all relevant ISAs in an audit of group financial statements. However, we do not believe that this should extend to duplicating issues that properly belong in other ISAs.

The proposal to develop a new standard for auditors who serve as component auditors is partly because it may be particularly useful to SMPs who may often operate in this capacity. We are, however, concerned that it may not be helpful because of the unavoidable level of duplication. However, we would support the IAASB considering a separate section in ISA 600 for component auditors.

The SMP Committee agrees that the ISA 600 cannot be too prescriptive requiring the nature, timing and extent of appropriate involvement of the group engagement team in the work of component auditors. It is important that the principles-based nature of the ISAs is maintained.

We do not support the IAASB exploring making reference to another auditor in an auditor's report. In our opinion, this may reduce the focus on the role and responsibility of the engagement partner and could affect the perception of audit quality as it may imply that the engagement partner is not as involved in the audit process. In addition, it may result in a lack of clarity over the responsibility of the auditors on the financial statements. The group auditor's primary responsibility for the group audit opinion should not be diminished, even if the component auditors are also providing an opinion on the respective group components.

**GA2. Acceptance and Continuance of the Group Audit Engagement**

***(a) Paragraphs 204–217 set out matters relating to acceptance and continuance of the group audit engagement.***



- (i) Which of the possible actions outlined in paragraphs 215–217 would be most meaningful in addressing issues related to acceptance and continuance procedures?**
- (ii) Why do you believe these actions are necessary?**
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.**

**(b) Specifically:**

- (i) Are access issues as described in paragraph 207(a) still frequently being experienced in practice? If yes, please provide details and, where possible, explain how these are being addressed today.**
- (ii) Do you agree that ISA 600 can or should be strengthened in relation to addressing access issues as part of acceptance and continuance?**
- (iii) Would expanding the understanding required for acceptance and continuance, as described in paragraph 215 (b), be achievable in the case of a new audit engagement?**

We believe that additional guidance could be added to support situations where there is likely to be significant complexity or difficulty in obtaining sufficient appropriate audit evidence, as well as for matters that may need to be considered in obtaining an understanding of the group, its components and the environment. In our opinion, group auditors need to be able to use their professional judgment about the work of component auditors and the quality of evidence provided.

We are not sure that providing examples of how access issues may be addressed in the application material will be that helpful because these may largely depend on local regulation and the individual circumstances. We would, however, support these being included in non-authoritative material such as a Staff Questions and Answers (Q&A).

The SMP Committee understands the intention of the Board is to strengthen the requirements covering obtaining a detailed understanding of the group, its components and their environments before deciding to accept or continue a group audit. However, it should be sensitive to situations where in certain circumstances an auditor may be unable to obtain information ahead of client acceptance, since such information will often not be equivalent to the sufficient, appropriate evidence required during an audit. It may transpire during the audit that a limitation of scope exists and a disclaimer opinion will be issued.



### **GA3. Communications between the Group Engagement Team and Component Auditors**

***(a) Paragraphs 218–225 set out matters relating to communications between the group engagement team and component auditors.***

- (i) Which of the possible actions outlined in paragraph 224 would be most meaningful in addressing issues relating to communication between the group engagement team and the component auditor?***
- (ii) Why do you believe these actions are necessary?***
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why?***
- (iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.***

We support the possible action to enhance the application material regarding communications between group engagement teams and component auditors. In particular, highlighting the value of sufficient and timely two-way communication during the audit. Additional guidance on what is meant by ‘timely’ and the examples of different kinds of communications that may be appropriate in different circumstances may be helpful, together with the importance of documenting significant communications.

There have been concerns raised over the timing, language used, and the level of detail that some firms require as standard practice as part of their methodologies for understanding the component auditors and work performed. This has been perceived by some as being purely a risk management exercise, rather than focusing on understanding the component auditor. Short response deadlines and excessive detail of information requested (which is disproportionate to the size, complexity and risk of the component) may actually impair the quality of the communication, information delivered and timeliness of the response by some SMPs. In addition, some SMPs have raised concerns about the lack of professional courtesy observed by group auditors in their interactions with component auditors. ISA 600 should encourage the proper tailoring of requests for information as it elicits a better quality of responses, together with group and component auditors agreeing on what, when and how information is provided.

The proposal to better address the ability of the group engagement team to communicate directly with a component auditor (or vice versa) when they are aware of non-compliance or suspected non-compliance with laws and regulations should be considered in the context of the final IESBA pronouncements which were finalized in April 2016.

### **GA4. Using the Work of the Component Auditors**

***(a) Paragraphs 226–242 set out matters relating to using the work of the component auditors.***



- (i) Which of the possible actions outlined in paragraph 234 and 242 would be most meaningful in addressing issues related to using the work of the component auditor?**
- (ii) Why do you believe these actions are necessary?**
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.**

**(c) Specifically:**

- (i) Should the nature, timing and extent of involvement of the group engagement team in the work of the component auditor vary depending on the circumstances? If yes, how could changes to the standard best achieve this objective?**
- (ii) (ii) Should ISA 600 be strengthened to require the group engagement partner to make an explicit determination about**

The SMP Committee believes that guidance in the application material that assists the group auditor to make an explicit determination about whether it is appropriate to use the work of a component auditor is more likely to be helpful than including an objective or new requirements. In this context we also refer to our response to QC 4(b).

We are concerned that developing application material to emphasize the need for the group engagement team to understand results of quality control monitoring may not be practical in all circumstances.

We are not convinced that there is a need to strengthen ISA 600 to provide more clarity as to how the group engagement team determines the nature, timing and extent of the necessary involvement in the work of the component auditors, partly because as the ITC acknowledges it cannot be overly prescriptive in establishing these interactions and the different approaches which may be appropriate.

We do not consider that extensive illustrative examples in ISA 600 would be particularly helpful. In our opinion, these detract from the principles based approach of the ISAs, but could be useful as separate material. This includes the proposals to include specific examples that address some of the practical challenges related to understanding the component auditor's compliance with relevant ethical requirements and to illustrate the wide variety of circumstances that may affect the determination of the necessary nature, timing and extent of the group engagement team's involvement in the work of the component auditor.



#### **GA5. Identifying and Assessing the Risks of Material Misstatement in a Group Audit**

**(a) Paragraphs 243–253 set out matters relating to identifying and assessing significant risks in a group audit:**

- (i) Which of the possible actions outlined in paragraphs 251–253 would be most meaningful to address issues relating to identifying significant risks for the group audit?**
- (ii) Why do you believe these actions are necessary?**
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.**

In our opinion, if the links that are stated as needed between ISA 600, ISA 315 (Revised)<sup>10</sup> and ISA 330<sup>11</sup> are included, so as to better support application of those ISAs in group audit engagements, then providing additional examples may not be required.

We agree that clarifying the application material to emphasize that significant risks identified by component auditors for a specific component should also be considered at the group level may be helpful. In addition, we support further clarification about how significant risks impact whether a component is considered significant and application material to further clarify the meaning of the phrase “of financial significance to the group”.

#### **GA6. Issues Relating to Component Materiality and Other Aspects of Materiality Relevant to Group Audits**

- (a) Paragraphs 254–261 set out issues relating to applying the concept of materiality in a group audit. Do you agree with the possible actions recommended in paragraph 261 to clarify the different aspects of materiality in a group audit? If not, please indicate which actions are not appropriate and describe why.**
- (b) Recognizing that significant changes to ISA 320 will not be contemplated until a review of ISA 320 has been performed in its entirety (potentially as part of a future project to address materiality more broadly), please describe any other relevant issues or additional actions that you think may be appropriate relating to component materiality, component performance materiality or the clearly trivial threshold at the component level.**

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<sup>10</sup> ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatements through Understanding the Entity and its Environment*

<sup>11</sup> ISA 330, *The Auditor's Responses to Assessed Risks*



The SMP Committee agrees that any actions taken in respect to ISA 600 should not infringe on the basic principles in ISA 320<sup>12</sup> and a future possible review of the standard. We agree that more guidance about how the concepts of component materiality and component performance materiality in the context of group audit are expected to be applied would be helpful, as long as the principles-based nature of the ISAs is retained.

**GA7. Responding to Identified Risks of Material Misstatement in a Group Audit (Including Issues Relating to the Group Engagement Team's Involvement in the Consolidation Process)**

**(a) Paragraphs 262–292 set out matters relating to responding to identified risk of material misstatement in a group audit (including the group engagement team's involvement in the consolidation process).**

- (i) Which of the actions outlined in paragraphs 272–273, 279, 288 and 292 would be most meaningful to address issues relating to responding to identified risks of material misstatement in a group audit?**
- (ii) Why do you believe these actions are necessary?**
- (iii) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (iv) Please also describe any potential consequences of possible actions that you believe we need to consider further.**

**(b) Specifically:**

- (i) What are your views on scoping the audit based on identifying and assessing the risks of material misstatement for the group as a whole, rather than focusing the determination of the necessary work effort on the determination of whether components are considered significant or non-significant? Are there any practical challenges that we need to consider further?**
- (ii) Are there other possible actions related to auditing groups where there are a large number of non-significant components that we should explore? Are there other approaches to auditing such groups that need to be considered? Do the possible actions presented lead to any additional practical challenges?**
- (iii) Should the standard be strengthened for the group engagement team to be more involved at the sub-consolidation level in the appropriate circumstances? Are there further issues or practical challenges that have not been considered?**
- (iv) Should the requirements or application material relating to subsequent event procedures be strengthened or clarified? Are there further issues or practical challenges that have not been considered?**

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<sup>12</sup> ISA 320, *Materiality in Planning and Performing an Audit*



The SMP Committee supports application material clarifying that the manner in which the requirement to perform “an audit of financial information of the component using component materiality” is applied may vary depending on the specific circumstances and may not necessarily mean the component is expected to apply all requirements in all relevant ISAs in all circumstances. For example, the group auditor’s risk assessment may be such that concentration on a component’s significant risks would provide sufficient appropriate audit evidence for the group auditor’s purposes. The component auditor would not necessarily need to perform a complete financial statement audit in such situations, but instead could be instructed by the group auditor as to their exact needs.

We therefore do not believe that examples of “specified audit procedures” or “specified procedures” in specific circumstances will be helpful as these will vary significantly. However, we support clarifying the expected work related to analytical procedures at the group level for non-significant components and the distinction between work performed for the purposes of the group audit and work performed to support a standalone auditor’s report at the component level.

We agree that reference to the cost method of accounting in the description of the consolidation process should be removed. In addition, we support clarifying that financial statements that only include investments accounted for at fair value or using the cost method of accounting are not considered group financial statements.

#### **GA8. Review and Evaluation of the Work of Component Auditors by the Group Engagement Team**

**(a) Paragraphs 293–303 set out matters relating to the review and evaluation of the work of component auditors by the group engagement team.**

- (i) Which of the actions outlined in paragraphs 299 and 303 would be most meaningful in addressing issues relating to the review and evaluation of the work of component auditors by the group engagement team?**
- (iii) Why do you believe these actions are necessary?**
- (iv) Are there other relevant issues that we should consider, or actions that would be more effective than those described? If you would not support a particular action, please explain why.**
- (v) Please also describe any potential consequences of those actions that you believe we need to consider further.**

We agree with the possible actions to address the issues identified. In particular, emphasizing the importance of ongoing two-way dialogue. In this context we also refer to our response to QC 4(b).

There is a risk in a group audit situation that working papers could be subject to excessive reviews or overly detailed reviews at different stages, so as to become disproportionate to the benefits in terms of enhanced



audit quality. The IAASB will therefore need to be careful to require reviews of working papers etc. are reasonable taken as a whole.

**GA9. The Impact of New and Revised Auditing Standards**

**How should the matters set out in paragraphs 304–305 be addressed in our plans to revise ISA 600?**

**Are there any other implications from our new or revised standards that should be considered?**

On balance the SMP Committee does not consider that there is a strong case for the Board to undertake any further action in relation to disclosures.

We believe that it would be helpful for application material relating to the communication of key audit matters ISA 701<sup>13</sup> to assist group engagement teams and component auditors. Due to their client base, many component SMPs may not be familiar with the reporting requirements under ISA 701, but may encounter a group level significant risk in the component entity. The group auditor will need to receive the necessary information on this area, should it be determined as a key audit matter for the group auditor's report.

**GA10. Are there any other issues relating to group audits that we have not identified? If yes, please provide details. What actions should we take to address these issues?**

We are not aware of any other issues relating to group audits that have not been identified.

**GA11. Are there any other specific actions that others could take in relation to group audits? If yes, please provide details.**

We are not aware of any other specific actions that others could take in relation to group audits.

**GA12. Are there any specific considerations for SMPs related to the issues and potential actions described in this section? Are there any other considerations for SMPs of which we should be aware? If so, please provide details and views about these matters.**

We have included comments above which highlight the importance that any changes being made to ISA 600 can be proportionally applied so as not to disproportionately impact SMPs who are often involved in larger group audits in the capacity of component auditor, as well as group auditor in the audit of smaller groups.

**GA13. Are there any specific public sector considerations related to the issues and potential actions described in this section? Are there any other public sector considerations of which we should be aware? If so, please provide details and views about these matters.**

We have no comments on public sector considerations.

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<sup>13</sup> ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*



## CONCLUDING COMMENTS

We hope the IAASB finds this letter helpful. We are committed to helping the Board in whatever way we can to build upon the results of this ITC.

Please do not hesitate to contact me should you wish to discuss matters raised in this submission.

Sincerely,

A handwritten signature in black ink, appearing to read 'Giancarlo Attolini', with a horizontal line above it.

Giancarlo Attolini  
Chair, SMP Committee