

Colin Semotiuk
Office of the Auditor General of Alberta
Edmonton, Alberta

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IAASB
529 Fifth Avenue
New York, NY 10017

Dear IAASB,

My response to exposure draft *Proposed International Standard on Auditing 600 (Revised)* is below:

Overall Questions

1. With respect to the linkages to other standards:

- (a) Does ED-600 have appropriate linkages to other ISAs and with the proposed ISQMs?

Overall, ED-600 is significantly linked to other ISAs. The linkages are extensive and pervasive. Given the pervasiveness of the linkages, the standard no longer stands alone. If the IAASB continues with the principles set in ED-600, it may be more efficient and effective to remove ED-600 and add individual sections to ISA 200, ISA 315, ISA 330, etc. on "*Auditing Group Financial Statements*." Such an approach would make the standards more understandable and easier for the IAASB to make amendments, if necessary.

- (b) Does ED-600 sufficiently address the special considerations in a group audit with respect to applying the requirements and application material in other relevant ISAs, including proposed ISA 220 (Revised)? Are there other special considerations for a group audit that you believe have not been addressed in ED-600?

ED-600 does not provide sufficient guidance on "*Using Audit Evidence from an Audit Performed for Another Purpose*" (ED-600.42). This situation is pervasive in the public sector where group auditors rely on independent component auditor's reports. In many situations within the public sector the component auditor is selected by an independent governing board or component management and not the group management or those charged with governance of the group financial statements. In Canada, a common example is school jurisdictions. The current ISA 600 meets the needs of these situations. ED-600 requirements are less

practical. For example, two competing firms may be involved as a group and component auditor. The component auditor will most likely have hesitation to allow the group auditor unimpeded access to their audit file (ED-600.A34). This methodology is part of their intellectual property and sharing this information with the group auditor when an independent auditor's report is issued on the financial statements may not be necessary. When an audit is completed in accordance with the ISA's, then this should be sufficient for a group auditor to place reliance on the component auditor's report.

Furthermore, the requirements in ED-600 of the group audit team to be involved in the work of the component auditor will not be practical in large (many component) group audit situations. Using the prior example of school jurisdictions, which in Canada are the jurisdiction of each individual province. It is not feasible for the provincial group audit team to be involved in the planning, execution and reporting of each individual school jurisdiction. ED-600 appears to have removed the concepts of significant and non-significant component. This concept aided group audit teams to focus on components based on risk. ED-600 has not maintained this guidance and has introduced increased requirements for involvement with component auditors and introduced group audit aggregation risk, making compliance with ED-600 strenuous.

In addition, ED-600 is not clear on what the audit team's requirements are when there is more than one level of component. What happens when a component has multiple components consolidated into it before it is consolidated into the governing entity? This situation is common in sectors such as education. ED-600.42 is also written in the past tense and not the present, why? In its current form, ED-600 is also not clear if statutory auditors are component auditors. This is due to the fact that ED-600.42 is in the past tense.

Another special consideration needed in ED-600 is guidance on the scope of ISA 600 regarding pension plans and the defined benefit pension liability that a sponsoring or participating entity may include in its financial statements, including related disclosures. Proposed paragraph ED-600.11 is not clear if the pension liability would be considered "consolidated" or not. If the pension liability (or asset) is not considered "consolidated," then ISA 600 does not apply, and the auditor would need to do all the audit work regarding the plan liability, which involves auditing plan assets, actuarial liability, etc. Often pension plans have their own audit, but as noted above ED-600.42 is unclear. As proposed, if the plan liability is not considered "consolidated," then the "group" auditor could not use ISA 600 for auditing the pension liability and would need to re-audit the plan. This would not be in the public interest. The situation is exasperated with the removal of ISA 600.02 of the existing standard (see comments under question 12 regarding the current 600.02).

2. With respect to the structure of the standard, do you support the placement of sub-sections throughout ED-600 that highlight the requirements when component auditors are involved?

As stated above, ED-600 does not provide sufficient guidance for using the work of component auditors and using audit evidence from an audit performed for another purpose, see response to 1(b).

3. Do the requirements and application material of ED-600 appropriately reinforce the exercise of professional skepticism in relation to an audit of group financial statements?

Yes, ED-600.05 and .A9-.A10 provide sufficient emphasis on professional skepticism.

Specific Questions

4. Is the scope and applicability of ED-600 clear? In that regard, do you support the definition of group financial statements, including the linkage to a consolidation process? If you do not support the proposed scope and applicability of ED-600, what alternative(s) would you suggest (please describe why you believe such alternative(s) would be more appropriate and practicable).

The scope and applicability of ED-600 is clear, however ED-600.08 states the objectives of the “auditor”. This could be clarified, specifically is this the objective of the “group engagement leader” or “group audit team.” Secondly, ED-600.08(d) states the auditor is required to “*evaluate whether sufficient appropriate audit evidence has been obtained from the audit procedures performed. . .*” It is not clear how this could be done without review of audit working papers. Application guidance should be provided as to what would be sufficient procedures to “*evaluate whether sufficient appropriate audit evidence has been obtained.*” If ED-600.23 & .A49-.A52 are applicable, they should be referenced in ED-600.08(d).

5. Do you believe the proposed standard is scalable to groups of different sizes and complexities, recognizing that group financial statements, as defined in ED-600, include the financial information of more than one entity or business unit? If not, what suggestions do you have for improving the scalability of the standard?

No, ED-600 does not appear scalable. As previously noted, ED-600 has removed the concept of significant component. The concept of significant component creates scalability and provides guidance when using audit evidence from an audit performed for another purpose.

Furthermore, how would ED-600 be applied with ISA 540? Is a group engagement partner or group engagement team required to complete the requirements of understanding an accounting estimate as required by ISA 540? Is the group engagement partner or group audit team permitted to delegate these requirements to a component auditor? The current ED-600 does not provide guidance on this issue.

Given the increased requirements on both the group engagement partner and group engagement team, ED-600 does not appear scalable.

6. Do you support the revised definition of a component to focus on the ‘auditor view’ of the entities and business units comprising the group for purposes of planning and performing the group audit?

I do not support the revised definition of a component auditor. ED-600's definition of a component auditor states "*A component auditor is part of the engagement team.*" This addition to the definition of a component auditor adds increased complexity and is a concern for multiple reasons. First, independence is separately governed in individual jurisdictions and many jurisdictions include prohibitions for the "engagement partner and firm." Due to the fact that independence rules correctly include "the firm," if the component auditor is included as part of the engagement team then the component auditor's firm would be prohibited from completing work for the entire group entity. In Canada this would create unnecessary difficulty. For example, firms audit many school jurisdictions across Canada which are consolidated into provincial government financial statements. If the firm is part of the consolidated provincial financial statements engagement team, as an auditor of an individual school jurisdiction, is that firm prohibited from providing their services to other consolidated entities, including health, government business entities, advance education institutions, etc.? Some jurisdictions may resolve this issue by having the rules of professional conduct provide a second definition of component auditor for independence considerations, however this creates increased confusion as the profession in that jurisdiction would be using two different definitions.

Second, by including the "*component auditor is part of the engagement team,*" a firm can take the position that "group engagement team" requirements within ED-600 are met when a component auditor completes the requirements because "*a component auditor is part of the engagement team.*" This creates the risk that the group engagement team will not complete all required procedures. Therefore, I recommend "*a component auditor is part of the engagement team*" be removed from the definition of component auditor.

7. With respect to the acceptance and continuance of group audit engagements, do you support the enhancements to the requirements and application material and, in particular, whether ED-600 appropriately addresses restrictions on access to information and people and ways in which the group engagement team can overcome such restrictions?

Overall I support the requirements of acceptance and continuance included in ED-600, however see the response provided to questions 1(b) when the component auditor and group auditor are not part of the same firm or associated firm.

8. Will the risk-based approach result in an appropriate assessment of the risks of material misstatement of the group financial statements and the design and performance of appropriate responses to those assessed risks? In particular, the IAASB is interested in views about:

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

Overall the responsibilities of the group engagement team are clear, however as previously noted they are not always practical, specifically with larger (multiple component) engagements. Unless the purpose of including the component auditor as "*part of the engagement team*" is that the "*group engagement team*" requirements are sufficiently met when either the component auditor or the group auditor complete the requirements. By ED-600 including the component auditor as part of the group engagement team, the group engagement team meets these

requirements through the work of the component auditor who is part of the group engagement team. Is this the IAASBs intention?

Another concern is how the “*group engagement team shall take responsibilities for the nature, timing and extent of further audit procedures*” (ED-600.33). Application guidance A86 - A90 is not clear when a component includes significant risk(s). In order to meet the current requirement and application guidance, I would expect the group engagement team would need to review the component audit working papers. This is another example that may not be practical with larger engagements that include multiple, sometimes 100’s of components. In these situations, it is common that the group auditor relies on an independent auditor’s report issued on the components financial statements. I encourage the IAASB to continue to permit this approach and update ED-600 accordingly.

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

See response to 8(a) above.

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

One practical challenge for the group audit team is how do they receive and respond to “*the results of the monitoring and remediation process or external inspections with respect to the component auditor’s firm.*” For example, PCAOB releases their inspection results approximately 18 months following the period reviewed. The PCAOB reports frequently include findings of deficiencies. In 2018, the large firms ranged from an 11.5% (6/52) Part I.A deficiency rate, to a 36.5% (19/52) Part I.A deficiency rate. It is not clear how a group auditor would respond to these deficiency rates.

9. Do you support the additional application material on the commonality of controls and centralized activities, and is this application material clear and appropriate?

Yes, overall the application guidance on common controls is clear, however ED-600.A63 states “typically, *the processing of transactions and related controls at a shared service center operate in the same way for all transactions regardless of the entity or business unit . . .*” This statement may not always be correct and frequently there can be key variations in controls that should not be overlooked by the engagement team and if the team uses this approach, their sample size would not be sufficient if they treat the controls as a single population. The guidance would be more beneficial if it stated, “*When the processing of transactions and related controls at a shared service center operate in the same way for all transactions regardless of the entity or business unit and the auditor has taken sufficient steps to confirm the operations of such controls . . .*”

10. Do you support the focus in ED-600 on component performance materiality, including the additional application material that has been included on aggregation risk and factors to consider in determining component performance materiality?

Yes, I agree that ED-600 should focus on component materiality. I encourage the IAASB to add more focus and clarity to ED-600. Specifically, ED-600 does not provide any guidance on how to calculate component materiality and states the “*amount shall be lower than group performance materiality*” and “*the component performance materiality amount for an individual component need not be an arithmetical portion of the group performance materiality and, consequently, the aggregate of the component performance materiality amounts may exceed group performance materiality.*” This creates a significant range in ED-600 compliant component materiality possibilities. For example, one firm may use the group performance materiality as component materiality as their general methodology. A second firm may calculate materiality for components as if they were separate entities, using standard materiality methodologies (0.5-1% of total revenues, 0.5-1% of total expenses or 1-5% of net income). A third firm may determine component materiality as a percentage of group performance materiality (e.g. 50-70% of group PM). These methods vary significantly and would result in a range of component materiality. Materiality should be clear to users and this principle should also apply to component materiality. Users should be able to anticipate the level of materiality used by the auditor as this is critical in the users understanding of the financial statements and auditor’s report. I encourage the IAASB to not only include the maximum component materiality amount, but to also include within the application guidance how to calculate component materiality and calculate an aggregate component materiality. This will add clarity to auditors applying ED-600 and increase understanding for the users of group financial statements, e.g. when immaterial errors are found, it will decrease the question – why didn’t the auditor find that?

11. Do you support the enhanced requirements and application material on documentation, including the linkage to the requirements of ISA 230? In particular:

- a) Are there specific matters that you believe should be documented other than those described in paragraph 57 of ED-600?

I have no additional matters that I would include to be documented however I think the IAASB should clarify where the documentation can be reasonably completed. Specifically for group audits when the component auditor is from the same firm. It would improve efficiency if the application guidance included, “*When the group auditor and component auditor are from the same firm, the group auditor may decide to document their compliance with ED-600.57 in either the group engagement team’s audit file or within the component auditors audit file. Such documentation may include the review of key position papers, meeting minutes and other key audit working papers.*” This approach would be appropriate to increase efficiency and avoid duplicate documentation.

- b) Do you agree with the application material in paragraphs A129 and A130 of ED-600 relating to the group engagement team’s audit documentation when access to component auditor documentation is restricted?

Yes I agree with application material in paragraphs A129 and A130.

12. Are there any other matters you would like to raise in relation to ED-600?

- ED-600.20(c) states that the group auditor shall receive “*prior to dating the auditor’s report . . . confirmation from the component auditors that the ethical requirements . . . including those related to independence, have been fulfilled.*” This would not be on a timely basis and would be too late if an independence threat or prohibition were identified. Confirmation of independence should be received by the group auditor prior to the component auditor completing any execution work on the audit (confirmation of independence should be included as part of planning). Further confusion is created by the fact, ED-600.20 is included under the “Acceptance and Continuance” section. Due to fact it is included under this section, is the group auditor required to receive two confirmations from the component auditor? One before the acceptance of the engagement and one “*prior to dating the auditor’s report*”?
- ED-600.A17 is unclear when ED-600 applies, for example would ED-600 apply when a component is immaterial or when the financial statements are consolidated with no component auditors? I would encourage the ISA to clearly state “*ED-600 applies for all consolidated financial statements,*” “*ED-600 applies only when the group audit team is using a component audit team*” or both. It would also be useful to clarify whether, for immaterial components, ISA 700.39 is intended to still apply and the auditor needs to communicate in the auditor’s report an additional description of their responsibilities.
- ED-600 does not include ISA 600.02 “*An auditor may find this ISA, adapted as necessary in the circumstances, useful when that auditor involves other auditors in the audit of financial statements that are not group financial statements. For example, an auditor may involve another auditor to observe the inventory count or inspect physical fixed assets at a remote location.*” This guidance is useful as it provided authority for a group auditor to use 600 when using a component auditor to complete specific procedures, such as an inventory count. ED-600 does not maintain this guidance. I encourage the IAASB to maintain (add back) the current ISA 600.02 within the revised 600 standard.

Request for General Comments

13. The IAASB is also seeking comments on the matters set out below:

- a) Translations—Recognizing that many respondents may intend to translate the final ISA for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents note in reviewing the ED-600.

Please see the Canadian AASB response for any translation concerns.

- b) Effective Date—Recognizing that ED-600 is a substantive revision, and given the need for national due process and translation, as applicable, the IAASB believes that an appropriate effective date for the standard would be for financial reporting periods beginning approximately 18 months after approval of a final ISA. Earlier application would be permitted and encouraged. The IAASB welcomes

comments on whether this would provide a sufficient period to support effective implementation of the ISA.

The IAASB has released a number of significant changes for the profession in the past 18 months, including ISA 540 and ISA 315. Additional significant changes are anticipated based on ISQM 1 and ISQM 2. I encourage the ISA to stagger the effective dates in order to provide sufficient time for firms and members to implement and learn the changes. Specifically, I encourage the ISA to leave 24 months between the implementation date of ISA 315 and ED-600. As ISA 315 is effective for audits of financial statements for periods beginning on or after December 15, 2021, I would not set an effective date before December 15, 2023. This approach may require an effective date greater than 18 months if ISA-600 (revised) is approved before June 2022.

Thank you for the opportunity to comment.

Sincerely,

Colin Semotiuk CPA, CA