

2 October 2020

The Chair
International Auditing and Assurance Board
C/- The International Federation of Accountants
529 5th Avenue
New York, New York
United States of America

Dear Sir

**Re: Exposure Draft – Proposed International Standard on Auditing 600
(Revised)**

On behalf of the Institute of Public Accountants (IPA), I submit our comments on the Exposure Draft (ED) – *Proposed International Standard on Auditing 600 (Revised) Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors and Proposed Conforming and Consequential Amendments to Other ISAs)*.

While the IPA supports many of the proposals in the ED, we have noted a number of enhancements and comments the IAASB should consider in finalising them:

1. Risk Based Approach to Identification of Audit Components – while we support the introduction of risk-based approach in ISA 600, we are concerned that the linkage of the existence of group audit to consolidation entries (in particular elimination entries) and the application guidance on centralised accounting functions are inconsistent with such an approach and would result in inappropriate outcomes
2. Linkages to Quality Standards – stronger links need to be made to the results of quality processes on the nature and extent oversight and review of component auditor workpapers included in both the revised ISA 600 and ISA 220 (Revised) *Quality Management for an Audit of Financial Statements*. Furthermore, ISA 600 and the ISQM 2 *Engagement Quality Reviews* should provide more guidance on the considerations governing the extent of the Engagement Quality Reviewer procedures in relation to review of component auditor work;
3. Centralised Services and Controls – while the IPA welcomes the incorporation of material relating to centralised operations and controls (including share services functions), the new guidance is rudimentary and should be enhanced

4. Communication between the Group Engagement Team and Component Auditors – the new guidance in the revised ISA 600 is in certain aspects (particularly component auditor instructions) inferior and not as useful as that in the extant ISA 600. The IAASB should re-examine this material for revision and incorporation into the revised ISA 600. The current guidance in relation to when a review of component audit work papers is required and the extent of such a review lack specificity
5. Constitution of the Group – the revised ISA 600 needs to specifically address minimum audit procedures required to determine the extent of the group i.e. the entities that should comprise the group financial statements
6. Consolidation Processes – the revised ISA 600 should provide more guidance on necessary procedures relating to consolidation processes, and
7. Offshoring – there is no guidance in either ISA 600 or other ISAs relating to the appropriate oversight and review procedures of the use offshore audit assistance in carrying portions of a financial statement audit and the IAASB should address this deficiency.

Our comments and responses to the questions in the ED are set-out in the Appendix to this letter.

If you would like to discuss our comments, please contact me or our technical advisers Mr Stephen La Greca (stephenlagreca@aol.com) or Mr Colin Parker (colin@gaap.com.au) GAAP Consulting.

Yours sincerely



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CC Chair, AUASB

About the IPA

The IPA is a professional organisation for accountants recognised for their practical, hands-on skills and a broad understanding of the total business environment. Representing more than 37,000 members in Australia and in over 65 countries, the IPA represents members and students working in industry, commerce, government, academia and private practice. Through representation on special interest groups, the IPA ensures the views of its members are voiced with government and key industry sectors and makes representations to Government including the Australian Tax Office (“ATO”), Australian Securities and Investments Commission (“ASIC”) and the Australian Prudential Regulation Authority (“APRA”) on issues affecting our members, the profession and the public interest. The IPA

recently merged with the Institute of Financial Accountants of the UK, making the new IPA Group the largest accounting body in the SMP/SME sector in the world.

Appendix A

Overall Questions

Question 1

With respect to the linkages to other standards:

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

IPA response

There is scope for improvement in relation to the linkages to other standards:

- ISQM 1 & ISA 220 – when considering the work of component auditors (including their selection and the degree of oversight and review of component auditor’s workpapers) there should be an explicit guidance on the impact of quality control process outcomes (e.g. internal and network quality control reviews) and regulatory reviews when determining the nature and extent of the review of component auditor’s conducted procedures
- ISQM 2 – there is insufficient guidance on the factors to be considered by the EQR to assist in determining the extent and nature of the review of component auditor’s workpapers and, in what circumstances, are reviews of component auditor’s reporting or the group engagement team’s review of component auditor’s reports/working papers sufficient
- ISA 300 – should include a reference to determining the scope of the group (i.e. what entities including structured entities, joint arrangements and associates are to be included). In addition, the proposed ISA 600 should include that group engagement team should consider providing, as part of the component auditor instruction package, the overall audit plan required to be produced by ISA 300, and
- ISRE 2400 – there are very few linkages in ISRE 2400 that provide specific consideration of the use of component auditors in a review engagement. ISRE 2400 needs specific guidance on the conduct of group review engagements, particularly in relation to the extent to which component auditors are required in a review, and when it is appropriate for the group engagement team to undertake review procedures on an audit component which would have been undertaken by component auditors in an audit engagement.

Question 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?

IPA response

No, we do not support the proposal. We are concerned that the result is cumbersome and particularly not user friendly where a group engagement is being carried audit by a single audit team.

The IAASB should split the standard into two parts comprising: group audit consideration; and component audit considerations.

Question 3

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

IPA response

No, the material in the ED does not particularly reinforce the exercise of professional scepticism as it is generic in nature (there are only two limited examples of professional scepticism issues applicable to group engagements) and largely consists of cross-references to other standards.

Specific Questions

Question 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).

IPA response

The IPA has concerns with the linkage to the consolidation process – it causes confusion and can lead to inappropriate conclusions in certain circumstances.

The emphasis on the existence of elimination entries (A18) is inconsistent with a risk-based approach to determining audit components. A group may consist of two or more divisions with distinct businesses, risks, internal controls and sharing a general ledger but with no intercompany transactions. The auditor may correctly determine the divisions are audit components on a risk basis (including assigning different audit teams to the operation divisions) but the lack of a consolidation process would result in ISA 600 not being applicable.

Similarly, the application guidance at A17 posits that where there is a centralised accounting function and no aggregation of financial information occurs ISA 600 is not applicable. This guidance and subsequent conclusion are also inconsistent with a risk-based approach. Sales, inventory and other systems and associated controls and management oversight may be divisional even where general ledgers and even payment systems are centralised. In such circumstances, a group audit approach may be applicable despite the existence of a shared services accounting function.

Question 5

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

IPA response

The proposals in the ED are scalable. However, as noted in our response to Question 2, the decision to include component auditor considerations as subsections make the standard cumbersome where the group audit will be conducted by a single engagement team.

Question 6

Do you support the revised definition of 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?

IPA response

The IPA supports the revised definition of a component based on an “auditor’s view”, however as noted in our response to Question 4, this definition is undermined by “overlay” of consolidation requirement (in particular the exitance of consolidation “eliminations”) and the application guidance at A17-A18.

Question 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?

IPA response

The IPA supports the amendments to client acceptance and continuance of group audit engagements where there are restrictions on access to information and people. We concur that there is no necessity to amend ISA 210 *Terms of Engagement* for the proposals in relation to group engagement client acceptance and continuance in the ED.

However, we are not satisfied that the application guidance in A32 and the revisions to ISA 705 provide adequate guidance in the body of the proposed ISA 600 to reflect the impact of an unresolved restriction on access to information or people in relation to an audit

component. While an illustrative example is referenced in the application guidance (A32) the standard itself should clearly enunciate the implications of such circumstances.

Question 8

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

- (a) Whether the respective responsibilities of the group engagement team and component auditors are clear and appropriate?*
- (b) Whether the interactions between the group engagement team and component auditors throughout the different phases of the group audit are clear and appropriate, including sufficient involvement of the group engagement partner and group engagement team?*
- (c) What practical challenges may arise in implementing the risk-based approach?*

IPA response

While the ED adequately addressed the respective roles the group engagement team and component auditors, the revised ISA 600 should clearly articulate the nature and content of instructions from the group engagement team. The IAASB should update and reinstate the existing ISA 600 Appendix 5 *Required and Additional Matters Included in the Group Engagement Team's Letter of Instruction*.

The application guidance at A113 relating to the review of component auditor's work papers is insufficient as it lacks specificity.

In addition, as noted in our response to Question 1, the group engagement team should provide the component auditor a copy of the overall group audit strategy.

The following issues are challenges to the proposed risk-based approach:

- Over reliance on centralised controls and processes by the auditor, resulting in reduced or no audit procedures carried out the component level particularly when there are significant non-centralised systems and processes e.g. sales, inventory control etc
- Over reliance on group management for representation and explanation of component results
- Rather than an audit centric model the auditor adopts the management/legal structure when determining audit components
- A reliance on management's assessment of component risk
- The failure to adequately determine the extent of the group e.g. the failure to include in the group structured entities
- Insufficient understanding of the individual components systems and how they interface with centralised systems including general ledgers, and
- Control knowledge concentrated on group systems, with little or no consideration controls implemented at the component level.

Question 9

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

IPA response

No, the guidance is at too a high level and of minimal practical use. Specific guidance is warranted on matters such as:

- The audit of a shared service component
- The necessity to understand the information “feeds”/interfaces to shared/centralised systems and where the responsibility lies for the completion and accuracy of such information, and
- The impact component management are responsibility for management oversight of shared data.

Question 10

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

IPA response

We support the introduction of the concept of performance materiality. However, the guidance at A73 and A74 is confusing. The last sentence of A73 states ‘However, this ISA does not require a different component materiality to be established for each class of transaction, account balance or disclosure for a component’ but A74 then describes when a different component performance materiality is required. The IAASB should modify the wording of A73 to better reflect the content in A74.

The IAASB should also address materiality considerations where an audit component may be required to produce separate financial statements. We aware of this is an issue for practitioners and there is diversity in practice.

While we support the approach taken to component materiality, we are aware of much confusion in practice between overall materiality, performance materiality and transaction/account-based materiality and their relationship with IASB accounting materiality. In particular, we note in determining performance materiality many auditors are using a standard “hair-cut” (say 15%) in determining performance materiality.

Question 11

Do you support the enhanced requirements and application material on documentation, including 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?*
- (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?*

IPA response

Except for the documentation relating to the communication between the group engagement team and component auditors as noted Question 8, we support the requirements and application material on documentation.

Question 12

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

IPA response

The IPA would like to raise the following issues that should be addressed as part of the revision of ISA 600:

- The revised ISA 600 should specifically address, as part of the group planning process requirements, for the group engagement team to determine the extent of the group (including structured entities, associates, and joint arrangements) exercising appropriate professional scepticism in doing so. We note that certain audit failures can be at least partly attributed to a lack of awareness of the extent of the entity to be audited
- Clarification of the applicability of revised ISA 600 to circumstances where the group engagement team and the component audit team are members of the same office. We are of the view ISA 600 should apply in such circumstances
- ISA 600 should provide more guidance in relation to the minimum audit procedures relating to the consolidation process, and
- The impact of using offshoring to carry-out audit procedures and the minimum level of oversight and review necessary to meet the requirements of the applicable auditing standards.

Request for General Comments

Question 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.*
- (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 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.*

IPA response

We have no comments in relation to translation matters.

An effective date for the revised ISA 600 18 months after approval is appropriate.