

Tom Seidenstein
IAASB Chair

Filed via the website

Brussels, 7 October 2020

Subject: Proposed ISA 600 (Revised): Special Considerations -- Audits of Group Financial Statements

Dear Sir, Dear Tom,

Accountancy Europe is pleased to provide you with its comments on proposed International Standard on Auditing 600 (ISA 600). We welcome the proposed revision of ISA 600 while acknowledging that it should not be seen as the only solution to ensure high quality group audits globally.

The Exposure Draft ISA 600 (ED-600) addresses relevant areas that, in our view, needed to be reconsidered when conducting group audits. In this regard, keeping in mind the intricacies of establishing a globally accepted set of requirements for a wide range of scenarios, we support the revision of the extant ISA 600 in a way to emphasize a risk-based audit approach to group audits.

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

We note that there are a few areas where practical implementation challenges may occur. The centralised, top-down approach as prescribed in the ED-600, whilst generally being welcomed to reinforce the role of the group engagement auditor, might have the counterproductive effect of discouraging the involvement of component auditors, especially when they are not in the same network. We fear that this could have implications on the audit market and on the level of competition in some countries in Europe. The significance of this issue very much depends on the jurisdiction and on the complexity of group audits that are considered.

Similarly, the top-down approach could, if not applied appropriately, reduce the ability of the group team to have a proper risk assessment and identification. Should the group engagement team perform the audit without component auditors as a systemic answer, in some cases, it could be detrimental to the quality of the audit. We elaborate on this issue in our response to question 8 and propose a way to address it.

The question of entry point is a very important issue which is up for interpretation in ED-600 for certain cases. This may lead to inconsistent application of the standard globally. We expand on this point in the specific questions below.

Finally, whilst our own outreach indicates support for the more flexible and principle-based concepts, this is also accompanied by a desire for more supporting guidance, particularly in respect of more complex group structures. Although this might not be a primary responsibility of the IAASB, we believe that the IAASB can play an important role helping to fill this gap, perhaps by engaging with IFAC and national standard-setters. Such an approach will help 'level-set' application expectations and mitigate the risk of inconsistent and jurisdictionally fragmented implementation. Without such supporting material we do not expect that challenges of very complex group structures will be overcome solely by revising the extant ISA 600.

We thank you for the opportunity to comment. For further information on this letter, please contact Noemi Robert on +32 (0) 2 893 33 80 or via email at noemi@accountancyeurope.eu.

Sincerely,



Olivier Boutellis-Taft
Chief Executive

ABOUT ACCOUNTANCY EUROPE

Accountancy Europe unites 51 professional organisations from 35 countries that represent close to **1 million** professional accountants, auditors and advisors. They make numbers work for people. Accountancy Europe translates their daily experience to inform the public policy debate in Europe and beyond.

Accountancy Europe is in the EU Transparency Register (No 4713568401-18).

ANNEX - REQUEST FOR COMMENTS

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?*
 - 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?*

a. Yes, ED-600 has appropriate linkages with other ISAs and proposed ISQMs. We agree that the requirements in ED-600 should build on requirements in the foundational standards and should focus on special considerations related to group audits.

b. In line with recently adopted ISA 220, ED-600 states that component auditors are members of the engagement team performing the group audit. This will lead to practical, and in some cases legal and regulatory, challenges related to the group engagement partner's responsibilities for direction, supervision, and review. This will be relevant particularly when component auditors are not in the same firm, or network. Whilst we do not disagree with the Board's underlying rationale driving this approach, the aforementioned practical problems could lead to both foreseeable and, as yet unidentified, application issues. We therefore recommend considering whether there is a better alternative way to avoid unintended consequences that we believe this 'group engagement team' approach brings.

Application material to ED-600 includes many examples of cases where common network policies, procedures and services can support the group engagement partner. This could be perceived as a bias towards group audits being performed by a single network. We do not believe that the Board intended this and including additional examples involving non-network component auditors would help portray a more balanced view.

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?*

Yes, the structure is helpful, especially for less complex group audits where component auditors are not involved. We see this as a positive contribution to the scalability of the standard, albeit this is not the only aspect of scalability. Please see our response to Question 5.

Notwithstanding the comment above, some of our members pointed out the risk of undermining or discouraging the involvement of component auditors by presenting relevant requirements separately. This structure could be perceived as promoting that the acceptable norm is not involving component auditors in group audits. Please see our response to Question 8.

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?

There is little harm in continuing to emphasise professional scepticism, however, we are not convinced that the requirements alone will significantly enhance its application. The stand back requirements referred at paragraph 97 of the Explanatory Memorandum, for instance already exist in the extant ISA 600.

On the other hand, we acknowledge that professional scepticism is not an issue that can fully be addressed by setting requirements in ISAs. In this regard, we believe the revised ISA 600 should focus

on group audit specifics, such as considerations related to unusual group structures and deciding on whether to involve the component auditors or not.

In addition to pure mind-set, the level of professional scepticism that can be applied depends to some extent on the information available to the audit team. Generally, the involvement of component auditors is likely to provide a broader view to the group engagement team, especially for large groups operating in various jurisdictions. Depending on facts and circumstances, a centralized approach without involving any component auditors might limit the application of professional scepticism and thus hamper audit quality. The group engagement team could have limited sources of information via the group's management without being able to corroborate the collected information with other sources of information via the component auditors. We suggest there is value in including this concept within the standard and linking it to the overall strategy decision regarding the use of component auditors. This is a good example of the benefits of using component auditors and the value of both top-down and bottom-up approaches to audit strategy.

Specific Questions

- 3. 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 explanations in the explanatory memorandum are clear. However, these are not fully reflected in the requirements of ED-600 leaving room for different interpretations.

There are certain threshold scenarios in which it will be problematic to find out whether ISA 600 applies or not - audits of letter box companies and shared service centres where there is no larger group as such are two examples. The IAASB could provide scenario-based application guidance to make sure the 'entry point' of the standard is clear across the board. Otherwise it will have to be prescribed in local jurisdictions, potentially by the interpretations of regulators. Hence, it could lead to fragmentation and inconsistent application of ISA 600.

As noted above, there are a number of corporate structures, legal and/or operational, that have used extant ISA 600 as a basis to develop their audit strategy, although these applications have often not been without any issue.

The identification of significant and non-significant components in the extant ISA 600 has been a fundamental part of group audits for many years and is considered to be effective by many practitioners. The removal of the requirement for full-scope audits of financial information for significant components could have huge implications in European jurisdictions where statutory audit is currently used as a mean to audit significant components. Therefore, we wonder if the IAASB could find a way to retain this by allowing auditors to follow a combined approach in cases where they find this more appropriate in meeting the objectives of the standard. More specifically, this could be achieved by adding a requirement for considering full scope of audit based on the significance of the component and other appropriate criteria.

- 4. 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?*

Yes, ED-600 provides improvement to the extant ISA 600 in terms of scalability. We acknowledge that developing a single standard that covers a wide range of scenarios from less complex entities to very complex group structures is a challenging task. As noted above, this necessitates more guidance on how the standard can be scaled up or down in the extreme scenarios. This is not necessarily a task for the IAASB but the IAASB could provide valuable facilitation.

On the other hand, some of our members are concerned about whether too much emphasis on the centralized and top-down approach may result in more work, and potentially less informed risk identification and assessment, at group level without necessarily enhancing audit quality.

5. *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?*

Yes, we support the flexibility provided to the auditor on how they view the group structure in order to design an efficient approach to planning and performing the group audit. We also believe that the group engagement team's consideration of the risks of material misstatement shall encompass all of the entities and business units that comprise the group as mentioned in paragraph A12.

This flexibility is in line with revised ISA 315 which has not become applicable in many jurisdictions yet. Hence, as the application of revised ISA 315 develops, this experience will help auditors adapt to the new approach proposed by ED-600 for group audits.

6. *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?*

We welcome the fact that ED-600 acknowledges this significant issue and urges auditors to consider potential implications in advance during the acceptance and continuance stage. We also agree that the implications of restrictions imposed by management and the ones outside their control should be distinguished and in any case the auditor's objective would be to obtain sufficient appropriate audit evidence.

We acknowledge that issues regarding accessibility cannot be overcome by an auditing standard. Hence the IAASB's mandate is limited and some operational aspects will eventually be solved depending on the circumstances of the local jurisdiction.

Nevertheless, the IAASB should work with stakeholders to better understand what "access" means considering today's evolving technologies. Based on this understanding, implementation guidance on how to deal with restrictions should be developed - for example, in the case of joint ventures and associates where access to information and people may be particularly challenging.

We also strongly agree that options to address accessibility should not be at the expense of audit quality.

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

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

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

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

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

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

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

Yes, we support the application material on the commonality of controls and centralised activities which are two different types of group-wide controls. They should be considered separately when obtaining an understanding of the entity and deciding on whether to rely on controls. The application material can be enriched by providing more examples on the factors to be considered when deciding on whether to rely on the controls and how to test them.

We do note however, that some of our members did not recognise the assumption that group auditors have been placing undue reliance on group-wide controls as asserted in paragraph 71 of the Explanatory Memorandum.

9. *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, we support the focus on component performance materiality. The relationship between the group materiality and component performance materiality is one of the areas which would benefit from implementation support.

10. 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?*
- 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?*

a. No, there are no other matters that should be documented in group audit engagements.

b. Yes. We agree that the group engagement team shall use professional judgment in determining relevant parts of the component auditor documentation to be included in the group engagement team's audit file.

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

As noted in our response to Question 6, the suite of enhancements to a number of ISAs have greatly elevated the focus on professional judgement and risk analysis. This is a welcomed move but is likely to need a period of experience to maximize the full value of the risk-based approach as prescribed in both ISA 315 (Revised) and ED-600. The objective of this approach is to help auditors design efficient and effective approaches and allocate their time on the areas with higher risk.

In order to achieve this, auditors need to understand the nature and the objectives of the new requirements. There will be some challenges for auditors to adapt to the new approach especially in the early years of application. Hence, implementation guidance clarifying fundamental changes would be very useful for a smooth transition.

Related to the earlier question regarding scope and entry point, we recommend the IAASB to consider retaining paragraph 2 of the extant ISA 600, as it does not appear in ED-600. Auditors may indeed find ED-600 useful when they involve other auditors in the audit of financial statements that are not group financial statements.

ED-600 rightly focuses on special considerations in audits of group financial statements, but its revision could have implications on the statutory audit at the component level. Moving from a component audit approach to a more risk-based approach, where more work is planned and performed by the group engagement team, could potentially lead to duplicate work and quality issues in the statutory audits at the component level as well. If a large proportion of the work is performed by the group auditor with the view to have an efficient group audit, there could be challenges associated with sharing the obtained audit evidence with the component auditor (statutory auditor). In multinational groups with regional shared service centers and competency centers it can be difficult to obtain audit evidence at the component level. It would be helpful if the IAASB could consider this issue further and address it in a separate standard or guidance.

Request for General Comments

12. 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 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.*

For the success of the implementation of the new standard, it will be important to give enough time for firms to digest it, and in particular to smaller firms which rely on off-the-shelf audit tool methodologies. This is particularly relevant considering the recently approved quality management standards that will need to be translated in the near future and then adapted.