This Staff Audit Practice Alert serves as an initial response to concerns raised by certain regulators and audit oversight bodies to audits in circumstances when the engagement partner is not located where the majority of the audit work is performed and reminds the auditors about how the ISAs address the responsibilities of the engagement partner in such circumstances.

Certain regulators and audit oversight bodies have expressed concerns related to audits in circumstances when the engagement partner is not located where the majority of the audit work is performed. In particular, the concerns expressed relate to how the engagement partner has taken responsibility for the direction, supervision, performance and review of the work, the adequacy of the audit documentation and whether, and how, the engagement partner has become satisfied that sufficient appropriate audit evidence has been obtained to enable the engagement partner to take responsibility for the auditor’s report. These regulators and audit oversight bodies have suggested that the IAASB take action as a matter of priority to address their concerns so as to enhance audit quality in these circumstances.

The IAASB’s Work Plan for 2015–2016 contemplates significant effort during the period on the topics of quality control and group audits more broadly. These topics have been identified as high priority projects relative to the IAASB’s strategic objectives for 2015–2019, in particular with respect to ensuring that the ISAs “continue to form the basis for high-quality, valuable and relevant audits conducted worldwide by responding on a timely basis to issues noted in practice and emerging developments.”

The IAASB therefore intends to seek further feedback on issues identified by regulators and audit oversight bodies during their inspections and about areas where auditors find it challenging to apply the ISAs, including further information about the circumstances addressed in this Staff Audit Practice Alert. Within the project on quality control, the IAASB will also explore how the engagement partner’s responsibilities are articulated within the ISAs and whether these responsibilities may need clarification.

Accordingly, a Discussion Paper is planned for later in 2015 to explore more holistically what actions the IAASB and others could take to enhance audit quality, including identification of potential areas for improvement within the ISAs. Feedback from this consultation will be used to determine the scope of standard-setting projects, including informing the basis for changes to the ISAs or additional guidance that may be necessary. For more information on these projects, visit the IAASB’s website at www.iaasb.org/quality-control and www.iaasb.org/group-audits.
BACKGROUND

The concerns of certain regulators and audit oversight bodies have largely been expressed in the context of some audits of financial statements of entities where the majority of the general and financial management of the entity and the majority of the business activities and related processing of transactions is located or undertaken in jurisdictions other than where the entity is registered or where the entity maintains a correspondence address or listing. The structure of these entities may be driven by requirements of taxation or other laws and regulations, or may be designed for the purposes of being able to more effectively raise equity or debt capital. In some cases, there may be limited investments or operations in the jurisdiction of registration or listing, with the majority of management and business activities being located or taking place in other jurisdictions. In these circumstances, the engagement partner may be located in the jurisdiction of registration or listing, with the majority of the audit work being performed in the other jurisdiction(s) where general and financial management are located and where the business activities and related processing of transactions takes place. Because the engagement partner is not physically located where the audit work is being performed, accomplishing the objectives of the ISAs in these circumstances, including addressing the requirements for taking responsibility for the direction, supervision, performance and review of the audit engagement, can pose different challenges than in situations where the engagement partner is located where the majority of the audit work is being performed.

KEY MESSAGES

The responsibilities of the engagement partner as set out in the ISAs apply to all audits, including in circumstances when the engagement partner is not located where the majority of the audit work is performed. This Staff Audit Practice Alert is intended to remind practitioners of the responsibilities of the engagement partner in those circumstances by focusing on certain requirements in the ISAs.

When auditing entities of all different structures, the focus of the engagement team, including the engagement partner, is the performance of a quality audit in accordance with the ISAs that supports the auditor’s conclusion that sufficient appropriate audit evidence has been obtained on which to base the auditor’s opinion. How the ISAs (in particular, ISA 220, ISA 230 and, when applicable, ISA 600) are applied to each audit engagement will vary based on the individual facts and circumstances due to the different structures of the entities whose financial statements are being audited.

- ISA 220 applies to all audit engagements that are conducted in accordance with ISAs, and ISQC 1 applies to all firms conducting these engagements.
- For audits of group financial statements, ISA 600 indicates that the group engagement partner applies the requirements of ISA 220 regardless of whether the group engagement team or a component auditor performs the work on the financial information of a component. In a group audit situation, the group engagement partner is therefore required to take responsibility for the direction, supervision, performance and review of the group audit engagement and for being satisfied that sufficient appropriate audit evidence has been obtained on which to base the auditor’s opinion on the group financial statements, regardless of whether the work is performed by the group engagement team or by a
APPLICABILITY OF THE ISAS

QUALITY CONTROL

The requirements in ISA 220 apply to all engagements that are conducted in accordance with the ISAs, including audits of the financial statements of the entities described on page 1.

ISA 220 establishes requirements for the engagement partner that are designed to facilitate a quality audit, including, among others, requirements for:

- Taking responsibility for the overall quality on each audit engagement to which that engagement partner is assigned.  

- Being satisfied that appropriate procedures regarding the acceptance and continuance of client relationships have been followed and determining that conclusions reached in this regard are appropriate.  

- Taking responsibility for (i) the direction, supervision and performance of the audit engagement in compliance with professional standards and applicable legal and regulatory requirements; and (ii) the auditor’s report being appropriate in the circumstances.  

- Taking responsibility for reviews being performed in accordance with the firm’s review policies and procedures.  

- Being satisfied, through a review of the audit documentation and discussion with the engagement team, that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued.
Group Audits

ISA 600 deals with special considerations that apply to group audits, in particular those that involve component auditors. ISA 600 notes that various types of entity structures may constitute a group. When an engagement is a group audit as defined in ISA 600, the requirements in that ISA apply.

ISA 600 assists the group engagement partner in meeting the requirements of ISA 220 in the context of a group audit.

ISA 600 explains that the group engagement partner is responsible for the direction, supervision and performance of the group audit engagement in compliance with professional standards and applicable legal and regulatory requirements, and whether the auditor’s report that is issued is appropriate in the circumstances. ISA 600 also notes that, although component auditors may perform work on the financial information of the components for the group audit and as such are responsible for their overall findings, conclusions or opinions, the group engagement partner or the group engagement partner’s firm is responsible for the group audit opinion.

In an audit of financial statements that are not group financial statements, but where other auditors are involved in the audit, ISA 600, adapted as necessary in the circumstances, may be useful to the engagement partner in planning and performing the audit in accordance with the requirements of the ISAs, including meeting the requirements of ISA 220.

Documentation

ISA 230 requires that audit documentation be prepared that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand:

(a) The nature, timing and extent of the audit procedures performed to comply with the ISAs and applicable legal and regulatory requirements, with specific elements required to be documented;

(b) The results of the audit procedures performed, and the audit evidence obtained; and

(c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

Audit documentation provides evidence that the audit complies with the ISAs, including that the engagement partner and, as applicable, the group engagement partner, has taken responsibility for the direction, supervision, performance and review of the engagement as required by ISA 220.

ISA 600 includes specific documentation requirements for group audits, including documentation of an analysis of components and the type of work performed on the financial information of the components; the nature, timing and extent of the group engagement team’s involvement in the work performed by the component auditors; and written communications between the group engagement team and the component auditors about the group engagement team’s requirements.
Responsibilities of the Engagement Partner in Circumstances when the Engagement Partner Is Not Located Where the Majority of the Audit Work is Performed

IAASB Main Agenda (June 2015)

ENDNOTES

i These entities have been referred to by some as “letterbox companies”.

ii Paragraph 7(d) of ISA 220, Quality Control for an Audit of Financial Statements, defines the engagement team as “all partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform audit procedures on the engagement…”

iii ISA 220, Quality Control for An Audit of Financial Statements

iv ISA 230, Audit Documentation

v ISA 600, Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)

vi International Standards on Quality Control (ISQC) 1, Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements

vii Paragraph 9(j) of ISA 600 defines the group engagement team as “partners, including the group engagement partner, and staff who establish the overall group audit strategy, communicate with component auditors, perform work on the consolidation process, and evaluate the conclusions drawn from the audit evidence as the basis for forming an opinion on the group financial statements.”

viii ISA 600, paragraph 5

ix ISA 220, paragraph 8

x ISA 220, paragraph 12

xi ISA 220, paragraph 15

xii ISA 220, paragraph 16

xiii ISA 220, paragraph 17

xiv ISA 600, paragraph A2

xv ISA 600, paragraph 1

xvi ISA 600, paragraph 5

xvii ISA 600, paragraph 11

xviii ISA 600, paragraph A8

xix ISA 600, paragraph 2

xx ISA 230, paragraph 8

xxi ISA 230, paragraph 9

xxii ISA 230, paragraph A7

xxiii ISA 600, paragraph 50