

**Group Audits – Discussion****Objectives of the Discussion**

The objectives of the discussion at the March 2015 IAASB meeting are to:

- Inform the IAASB about the history of the revision and redrafting of ISA 600 during the clarity project, as well as to discuss more recent issues and concerns about the standard that have been identified.
- Obtain the Board's views on the way forward to the development of a project proposal, including the issuance of a Discussion Paper (DP).
- Request input on, and support for, the Working Group's proposed approach to addressing letterbox audits.

**Introduction**

1. The International Auditing and Assurance Standards Board's (IAASB) *Strategy for 2015–2019* acknowledges the IAASB's strong commitment to meeting the expectations of stakeholders regarding the application of the International Standards on Auditing (ISAs). Accordingly, the IAASB has agreed to focus on certain ISAs in 2015–2016, including planned efforts on group audits that commenced with forming a Working Group in 2014.
2. As the Working Group commences its activities, it has developed this paper to provide the basis for exploring the initial way forward on this project with the IAASB. The content of the paper is intended to provide the IAASB with information about issues and concerns that have been identified related to the implementation and use of ISA 600<sup>1</sup> in group audits and the history of ISA 600, including significant decisions that were made in revising and redrafting the standard during the clarity project. There is also a separate section to address letterbox audits that builds on the discussion held with the Board in December 2014, and includes the Working Group's suggestions for the next steps.

**Structure of This Paper**

3. This paper has been set out in the following sections:
  - Section A—Background to This Project
  - Section B—History of ISA 600
  - Section C—Proposed Way Forward
  - Section D—Letterbox Audits – Proposed Way Forward

**A. Background to This Project**

4. ISA 600, as revised and redrafted, was published in October 2007 and was effective for periods beginning on or after December 15, 2009.

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<sup>1</sup> ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

5. At that time, the IAASB undertook various implementation activities to assist auditors in implementing<sup>2</sup> the revised and redrafted standard, including:
  - (a) A [video presentation](#) (with relevant slides), released in 2009.
  - (b) An [IAASB Q&A](#) to address an identified issue relating to the application of the International Ethics Standards Board's *Code of Ethics for Professional Accountants (IESBA Code)* to component auditors. Clarification was provided that the IAASB did not intend to extend, or otherwise override, the independence requirements of the IESBA Code or other ethical requirements to which the group engagement team is subject. This clarification has now been included in ISA 700 (Revised),<sup>3</sup> paragraphs A33–A34, as part of the revision of ISA 700 in the Auditor Reporting project.
6. In making the decision that a project on group audits should be a priority for the Board in the 2015–2016 period, consideration was given to the findings from the ISA Implementation Monitoring project, input from stakeholders, including some regulators and audit oversight bodies, the responses to the IAASB's Consultation Paper on its Future Work Plan for 2015–2016, and other sources. Each of these is described in more detail below.

#### **I. ISA Implementation Monitoring Findings**

7. In its *Strategy and Work Program 2009–2011*, the IAASB committed to undertake the development and implementation of a process for assessing the effectiveness of the implementation of the clarified ISAs (including the revised and redrafted ISA 600), to assist the IAASB in determining whether there was a need for further refinement in the clarified standards in order to achieve their intended objectives. This project was carried out in two phases and is explained in more detail below.

##### *Findings from Phase One of the IAASB's ISA Implementation Monitoring Project*

8. In November 2010, the IAASB released an interim report on Phase One of the review, [Implementation of the Clarified International Standards on Auditing \(ISAs\)](#). The objective of Phase One of the project was to obtain information about the pre-implementation experiences of introducing the clarified ISAs into national standards or firm methodologies to help provide early indications of:
  - (a) Areas of difficulty regarding use of the clarified ISAs.
  - (b) Areas where there is a need for additional guidance.
  - (c) Other actions to facilitate the successful implementation of the standards.

Information that was summarized in the report was primarily obtained from survey questionnaires completed by eight larger firms and by eleven countries participating in the IAASB's National Auditing Standard Setter (NSS) Liaison group.

9. The interim report on the findings from Phase One of the review set out both the findings and a response from the IAASB. Findings relating to ISA 600 included:

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<sup>2</sup> Many firms also developed tools and practice aids to help with the implementation of the revised and redrafted standard.

<sup>3</sup> ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

- (a) A number of firms raised issues relating to applying the requirements of ISA 600 to a significant component that is accounted for under the equity method in accordance with the applicable financial reporting framework.<sup>4</sup>
  - (b) Access issues by the group auditor to the relevant information of the component in some circumstances, with the result that the auditor's report is required to be modified, and in some jurisdictions the listing authority does not accept a modified auditor's report.
10. The IAASB acknowledged the need for consideration at the planning stage about whether and how the auditor would be able to direct, supervise and perform the group audit engagement to obtain the necessary audit evidence, but was of the view that it would be rare that the group auditor would not be able to have sufficient involvement in the audit work being performed at the component level. Notwithstanding this view, the IAASB requested the Forum of Firms (FoF) to provide more information about the practical implications and problems experienced on 2010 audits. In addition, the six largest FoF members developed an internal publication to highlight the issues and encourage early discussions with client management or those charged with governance (TCWG), as appropriate, to help avoid potential problems on a timely basis. The last update to this internal guidance was in 2012.

*Findings from Phase Two of the IAASB's ISA Implementation Monitoring Project*

11. In 2011 and 2012, the IAASB carried out activities on Phase Two of the ISA Implementation Monitoring project. Phase Two was comprised of a post-implementation review of the ISAs to determine whether there was any need for further refinement to achieve the intended objectives of those standards. The review therefore focused on whether the clarified ISAs were being implemented in a way that the IAASB had hoped, or whether there was a need for further refinement of those ISAs.
12. In July 2013 the report on the findings, [\*The Clarified ISAs—Findings from the Post-Implementation Review\*](#) (the Report), was published. The IAASB also agreed that the significant findings from this review would be considered for prioritization in its future strategy and work plan commencing in 2015.
13. Although not specific to ISA 600, overall comments made by respondents in the ISA Implementation Monitoring project acknowledged that improvements had been made in the clarified and redrafted standards, in particular that they were more clear and understandable. Concerns were expressed about the inconsistent application of some standards, but it was noted that the revised and redrafted standards focused auditors more on the risks. Due to the nature of the outreach as part of the ISA Implementation Monitoring project, the majority of respondents commented on specific areas where the standards could be improved, or where there were concerns that the standards were not being implemented as intended. The Report focused on these comments, and the summary below is an extract of those reported findings relating to ISA 600.
14. In order to analyze the comments received, the IAASB grouped related comments from the responses by ISA under relevant "themes". The IAASB prioritized the themes based on the following criteria:

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<sup>4</sup> This issue has also been highlighted in Phase Two of the ISA Implementation Monitoring review, see paragraph 18 of this paper.

Criteria	
<b>Key</b>	There is a body of evidence to suggest that the ISA is not being consistently understood and applied in a manner that achieves the IAASB’s goals in revising it. Changes to the ISA are likely to have the greatest potential for improving audit quality.
<b>Important</b>	There is some evidence to suggest that the ISA is not being consistently understood and implemented in a manner that achieves the IAASB’s goals in revising it. Changes to the ISA may have potential for improving audit quality.
<b>Other</b>	There is limited evidence that suggests that a change to the ISA may have merit.

15. In relation to ISA 600, the findings,<sup>5</sup> in summary, included:

Key Themes	Important Themes
<p>Many concerns were raised in relation to inconsistency in the degree to which the group auditor becomes involved in the work of component auditors.</p> <p>Also of concern is the inconsistency in the determination of component materiality, and the resulting impact on the work effort.</p>	<p>Concern was expressed about the application of ISA 600 in relation to:</p> <ul style="list-style-type: none"> <li>• The approach to material equity investments;</li> <li>• When the engagement partner is at a different location from where the vast majority of the audit work is performed; and</li> <li>• “Fund of funds” audits.</li> </ul>

Key Themes<sup>6</sup>

16. Group Auditor’s Involvement in the Work Performed by Component Auditors

A wide range of respondents, from both the accounting profession and audit inspection bodies and other regulators, suggested that there is inconsistency in the extent to which group auditors involve themselves in reviewing the work of the component auditor, and evidencing the work that they have performed on the component auditor’s work. Areas suggested for further consideration included the need for the IAASB to be more specific on:

- The level of understanding needed of components, especially where the environment of the component is very different from the domestic environment (e.g., in relation to business practices, legal structures, law and regulations, and customs);

<sup>5</sup> There were also “other” themes that were noted in the Report that will be considered in the project, but the focus will be on the “key” and “important” themes as highlighted above. More detail on the “other” themes has been presented below.

<sup>6</sup> The detail of the themes identified in this section have largely been extracted from the *Clarified International Standards on Auditing — Findings From the Post-Implementation Review* report.

- The level of understanding needed about the competence and independence of the component auditor including, for firms in the same network, how much reliance is to be placed on quality control systems;
- The need for the group auditor to document the extent and nature of their involvement in the work of component auditors, and why they consider it to be appropriate;
- The need for more specific guidance on when the group auditor needs to review the working papers of a component auditor, the nature of the review and how to evidence the extent and nature of that review;
- The group auditor’s work on the consolidation process; and
- The extent to which the group auditor specifies group risks to component auditors and the meaning of “significant risks” in a group context.

#### 17. Component Materiality<sup>7</sup>

Several respondents noted that there is significant variation in practice relating to the determination of component materiality. As a result, component materiality may be set too high and therefore insufficient work may be performed on the components. Some suggested that the rationale for setting component materiality below group materiality may not be well-understood.

#### Important Themes

#### 18. Application of ISA 600 in Certain Situations

Questions have been raised about the applicability and, if applicable, the practicality and cost effectiveness of ISA 600, in certain circumstances including:

- When an equity investment or joint venture is a significant component.  
  
Concern has been raised that ISA 600 does not provide sufficient guidance when the auditor does not have access to relevant information (for example, if the group auditor has no legal right of access to management and the accounting records of a company that is an equity investment), and that the (component) auditor of the investee has no legal obligation to cooperate with the group auditor. These issues are compounded if the reporting dates are different.
- When the engagement partner is in a different location from where the vast majority of the audit work is performed.<sup>8</sup>

There are mixed views on whether ISA 600 applies when the group opinion is signed by a partner in a jurisdiction different from where the group’s operations, accounting records and management are located, and hence where a vast majority of the underlying audit work is performed.

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<sup>7</sup> As the IAASB progresses its work on group audits, consideration will be given to those aspects of component materiality that may be better addressed in a more holistic review of ISA 320, *Materiality in Planning and Performing an Audit*. The Basis for Conclusions for the IAASB’s *Work Plan for 2015–2016* highlighted this as a potential project for the 2017–2018 Work Plan.

<sup>8</sup> These are also referred to as “letterbox” audits – see Section D for more on letterbox audit considerations.

- When the audited entity is a “fund of funds” structure.

A few respondents questioned whether ISA 600 applied to the financial statements of a “fund of funds” structure, and called for guidance on what is considered sufficient appropriate audit evidence in these situations. A small number of other audit issues were identified in relation to collective investment schemes.<sup>9</sup>

#### Other Themes

19. Communication Between the Group Auditor and Component Auditors.

Views were expressed that communication between the group and component auditor needs to be more consistent.

20. Acting as a Group Auditor.

It was questioned whether ISA 600 is specific enough as to how to determine whether an auditor is entitled to act as the group auditor.<sup>10</sup>

21. What is Meant by “An Audit” of Component Information in Some Cases.

It was questioned whether the “audit of a component” requires all the ISAs to be applied (for example, if it is not a statutory audit and only one for the purpose of a group audit, do standards such as ISA 700 (Revised) apply)?

22. Definition of a Component.

In the current environment where businesses are operating in integrated structures, the view was expressed that there is inconsistent application of ISA 600 due to the different interpretations of the definition of a component. In particular it was noted that branches and shared service centers give rise to difficulty, as well as where the financial reporting structure of the organization differs from its legal structure. This has resulted in an inconsistency in the work effort depending on whether the function has been identified as a component or not.

23. Work Effort Where There are No Significant Components.

There was a call for further guidance to be provided on how to scope the group audit when there are no significant components and a rotational approach to selection of components at which to perform procedures is adopted.

24. Meaning of “Specified Audit Procedures”.

It was suggested that additional guidance should be provided.

## II. Regulatory Input and Audit Inspection Findings

25. Increasing interest of the regulators and audit inspection groups in the IAASB’s standard-setting activities, and their interest in providing greater input at the commencement of the IAASB’s planned new projects, including the group audits project, has prompted more interaction with various groups and individuals in varying capacities.

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<sup>9</sup> Also referred to as “Fund of funds” audits

<sup>10</sup> It was suggested that additional guidance was needed to determine when it may be appropriate for an auditor to act as the group auditor if a significant portion of the consolidated information was audited by other component auditors.

26. The Working Group understands that concern over the implementation of ISA 600 has been a consistent theme or finding in many audit inspections conducted by different regulators and audit inspections groups. The Working Group has looked to various sources to obtain further information about audit inspection findings related to group audits. This included various meetings of IAASB leadership with such groups as the International Forum of Independent Audit Regulators (IFIAR) (including its Standards Coordination Working Group), the European Audit Inspection Group and the International Organization of Securities Commissions' (IOSCO) Committee 1 and Audit Subcommittee, as well as informal discussions with individual regulators in which their individual views and perspectives have been provided. In the Working Group's view, the overarching theme of inspection findings and where many regulators and audit inspectors have expressed concerns, relates to the involvement of the group auditor in the audits of components and over-reliance on the component auditor. It has, however, been acknowledged that there is also a wide array of practice in this area, and that some group audits inspected were carried out in accordance with the standard.
27. The Working Group has attempted to summarize below its understanding of the most significant concerns expressed to date by audit oversight bodies relating to group audits. These represent areas where some audit inspectors have expressed concerns, but it should be noted that these are not necessarily issues on every group audit or concerns that would be expressed by every audit inspector. The nature of audit inspection findings is that they focus on identified areas common to a number of audits selected for inspection, but they are not necessarily representative of all audits or all audits selected for inspection. The Working Group anticipates that continued dialogue with regulators and audit oversight bodies will facilitate a further understanding of the concerns as well as their pervasiveness.

#### *Planning Phase*

- In some instances, the group auditor has not obtained a proper understanding of the group to be able to “drive” the audit.
- In some cases, inadequate consideration about the acceptance and continuance of group audit engagements, and the related appropriateness of the group auditor to undertake the group audit engagement (for example, assessing that the group auditor would be able to obtain sufficient appropriate audit evidence on which to base the group opinion).
- In some cases, there has been insufficient assessment of the competence of the component auditor by the group auditor. This may include inadequate:
  - Evaluation of the component auditor's skills necessary for the audit of the component (e.g., the component auditor may need to have industry-specific knowledge or have sufficient knowledge of the applicable financial reporting framework under which the group is reporting);
  - Understanding and evaluation of the quality control monitoring results for the component auditor; or
  - Understanding of the licensing requirements for the component auditor (including the component auditor's compliance with these requirements).
- In some circumstances, the group auditor did not appropriately identify significant components, with the result that there was an inappropriate work effort on these components.

- Inadequate assessment by the group auditor of the risks of the engagement, including identifying the risks that are specific to individual components. For example, some regulators noted instances where the group auditor had not adequately identified certain risks, such as those that may be specific to the country or jurisdiction in which the component operates, or had not appropriately addressed the implications for the group audit when audit inspection findings of network firms in relation to International Standard on Quality Control (ISQC) 1<sup>11</sup> have identified significant deficiencies.
- In some cases, the group auditor did not appropriately take into account aggregation risk because materiality to be used by component auditors when performing work at selected components was not determined appropriately (a wide variation of practice in this area was noted).
- Additionally, the planning of the audit did not always include appropriate audit procedures to address insignificant components not selected for testing, where such components collectively represent risks of material misstatement to the group financial statements.
- Inadequate planning for sufficient involvement in the work of the component auditors, including site visits and review of the component auditor's planning procedures (at the planning stage of the audit).

#### *Execution and Completion Phases*

- In some cases, there has been insufficient communication between the group auditor and the component auditor. A possible reason could be that there is no requirement in ISA 600 for a “feedback loop” during an engagement whereby the group auditor and the component auditor discuss and agree the approach to the audit and subsequent to the performance of procedures by the component auditor, the group auditor reviews and discusses this work with the component auditor. For example, this may result in the need for the group auditor to make site visits to the component auditor. Inadequate communication may lead to the potential for misunderstanding between what is being requested by the group auditor and the work effort and findings of the component auditor. There may also be cultural or language issues related to inadequate communication between the group and component auditor, for example, in some jurisdictions there may be restrictions on the extent to which component auditors may communicate audit findings.
- In some instances, overreliance on the component auditor for procedures performed in areas such as the consolidation of financial information has been identified.
- Review by the group auditor of the component auditor's procedures and the results of those procedures has been identified in some group audits as being insufficient. In some of these cases, there is insufficient documentation of this review. Concern has also been expressed by some regulators that in some cases too much reliance is placed on “inter-office” clearance memos.

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<sup>11</sup> ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Service Engagements*

- Insufficient consideration of the effects on the group audit of the component auditor’s findings, including the evaluation of whether sufficient appropriate audit evidence has been obtained as a whole.
28. Some inspectors are of the view that the common root cause of these issues is insufficient involvement by the group engagement partner in the work of the component auditors. In particular, some of these inspectors believe that the ISAs are not prescriptive enough in describing the necessary involvement.

### III. Other Inputs

29. Other issues or concerns relating to group audits have been identified in the IAASB’s ongoing, or recently completed, projects. For example, responses to the Exposure Draft (ED), [\*Proposed Changes to the International Standards on Auditing \(ISAs\)–Addressing Disclosures in the Audit of Financial Statements\*](#), suggested the possible need for additional guidance in ISA 600 to address auditing disclosures in the context of group audits, as follows:

- A few respondents suggested that guidance could be included to facilitate the earlier consideration of disclosures in the reporting and consolidation process of a group audit (in particular the impact of component disclosures on the relevant materiality of group disclosures), thus properly addressing the impact of component financial statement disclosures on the group financial statements. Respondents also suggested that the discussion among group engagement team members and component auditors regarding the risk of material misstatement of the group financial statements should also include consideration of the disclosure requirements of the applicable financial reporting framework.
- One respondent suggested that auditors may face greater challenges when accumulating uncorrected misstatements in a group audit, especially for qualitative disclosures, and therefore additional guidance in this area would be welcome, including how the group auditor should communicate the threshold for reporting of uncorrected misstatements relating to qualitative disclosures to the component auditors.

The IAASB agreed that consideration should be given to the inclusion of additional application material in ISA 600 to address these issues as part of the project to revise ISA 600.

30. In addition, as the IAASB commences its work plan for 2015–2016, it is likely that other planned projects on Quality Control, professional skepticism, and others may identify issues that will cross-over into ISA 600 and the group audits project.

#### *The IAASB’s Work Plan for 2015–2016*

31. In light of the feedback on its Consultation Paper, in which group audits was not originally proposed as one of the priority projects for the 2015–2016 Work Plan, the IAASB reassessed its original approach to address three priority projects on an accelerated basis and to commence work on more projects than initially envisaged in the 2015–2016 period. In particular, the decision was made to accelerate substantive work on group audits, among other projects brought forward.
32. As part of its deliberations, the IAASB agreed to initially seek an understanding of the issues relating to “letterbox” audits and the approach to such audits, including the applicability of ISA 600 in such circumstances. Work on this commenced in 2014, with initial discussions with the IAASB’s Steering Committee, followed by Board discussions in December 2014. Further discussion on the way forward

on this aspect, as well as a summary of the Board's decisions in December 2014, can be found in Section D.

**Matter for IAASB Consideration**

1. Are there any other inputs or issues relating to ISA 600 that the IAASB believes the Working Group should further explore as relevant background for the new project?

**B. History of ISA 600**

*[The intent of this section is to provide background information about the decisions that were made to finalize ISA 600, and therefore inform the IAASB as to the various changes that were made as the standard was developed. This section should be read in conjunction with the Appendix, which sets out detail about the three ED's issued.]*

33. In the early 2000's, certain audit failures highlighted the need for the auditor of group financial statements to be more involved in the audit of group entities (e.g., Parmalat).<sup>12</sup> Several bodies, in particular the European Commission, IOSCO, the former Panel on Audit Effectiveness in the United States, and the International Forum on Accountancy Development, highlighted the need in the ISAs for more guidance on the audit of group financial statements, and requested that consideration be given to this matter. In particular, the EC emphasized that strengthening of the auditing standards relating to audits of group financial statements, together with the changes being made in the Clarity project, would assist with the adoption of the ISAs in Europe. Accordingly, the predecessor of the IAASB, the International Auditing Practices Committee, commenced a project on the audit of group financial statements.
34. In developing the standard, the IAASB issued three ED's. The Appendix sets out the pertinent decisions from the ISA 600 EDs issued in 2003, 2005 and 2006 to provide a history of the evolution of the standard. A summary of the final decisions, as presented in the Basis for Conclusions for the final standard, is presented below.

*Final ISA 600 as Issued*

35. As the ED's were developed, the group engagement team's procedures were strengthened, both in respect of the direction of the audit by the group engagement team and the group engagement team's involvement in the work of component auditors. Due to significant variances in group audit practices, the IAASB worked towards developing requirements and guidance capable of consistent application through specificity about the group audit engagement team's procedures.

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<sup>12</sup> The Parmalat scandal came to light in 2003 following the discovery of a significant deficit in finances and considerable fictitious assets held at Bank of America. US creditors filed a class action suit against Parmalat's former auditors and bankers and Parmalat's administrators sued Bank of America, Citigroup, Deloitte and Touche and Grant Thornton. This scandal highlighted the interaction between the group auditor and a component firm from another network.

36. The following sets out the final decisions made by the IAASB in finalizing the standard, largely based on the responses to the proposals in ED 2006:

#### Objectives

- (a) Revise the “Objectives” to make clear that it includes clear communication with component auditors, as well as obtaining sufficient appropriate audit evidence regarding the financial information of components and the consolidation process on which to base the audit opinion.

#### Definitions

- (b) Revise the definition of “component” and its related application material to recognize that some entities may not report information based on a typical organizational structure and that, in these situations, a component may be determined to be something other than a legal entity.
- (c) Develop further application guidance to explain that the structure of a group affects how components are identified.

#### Group Engagement Partner, Group Engagement Team and Component Auditor

- (d) Make a clearer distinction between the group engagement partner<sup>13</sup> and the group engagement team, and align the definition of group engagement partner in the ISAs with the definition of “engagement partner” in the IESBA Code. (See development of these changes in ED 2003 (paragraph 4(f)), ED 2005 (paragraph 8(b)) and ED 2006 (paragraph 11) in the Appendix)

#### Full versus Divided Responsibility

- (e) Make clear within the requirements that the group engagement partner is responsible for the direction, supervision and performance of the group audit engagement in compliance with professional standards and regulatory and legal requirements, and whether the auditor’s report that is issued is appropriate in the circumstances, to address concerns that the status of the Introduction section (where such material had previously been included) did not sufficiently underpin the importance of the assertion.<sup>14</sup> (See further decisions related to this in ED 2003 (paragraph 4(e)) and ED 2005 (paragraph 7) in the Appendix)

#### Acceptance and Continuance of Group Audits – Access to Information

- (f) Continue to require the group engagement partner to have a reasonable expectation of obtaining sufficient appropriate audit evidence on which to base the audit opinion before accepting or continuing a group audit engagement,<sup>15</sup> but to limit this to cases where the

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<sup>13</sup> The March 2006 ED still referred to the “group auditor.” The IAASB made changes in the final standard to distinguish the group engagement partner and group engagement team to address concerns about members of the engagement team being responsible for the tasks devolved to the group engagement partner. This would help ensure that requirements to be fulfilled by the group engagement partner should be addressed by the group engagement partner.

<sup>14</sup> This reinforced the IAASB’s decision to no longer allow for ‘divided’ responsibility for the group audit opinion.

<sup>15</sup> All three ED’s reflected the IAASB’s view that a restriction on the group engagement team’s access to relevant information is a scope limitation, which may affect the group audit opinion.

restrictions are imposed by management.<sup>16</sup> (See further decisions related to this in ED 2003 paragraph 4(c), ED 2005 (paragraphs 8(a) and (d) and ED 2006 paragraph 12)

#### Materiality

- (g) Emphasize that the requirements and guidance only apply in the case of the audit or review of a component performed for the purpose of a group audit at the request of the engagement team.
- (h) Retain the requirement for the group auditor to determine materiality for the group financial statements as a whole, and an amount or amounts lower than group materiality for the financial statements as a whole for the purposes assessing the risks of material misstatement and designing further audit procedures to respond to assessed risks at the group level (referred to as “component materiality”.)
- (i) Delete the requirement for the group engagement team to determine an amount(s) lower than the component materiality for the purposes of assessing the risks of material misstatement of the financial information of the component and to design further audit procedures (i.e., performance materiality at the component level). Rather, the group engagement team should be required to evaluate the appropriateness of any such amount(s) determined at the component level (by the component auditor).

#### Significant Components

- (j) Amend the requirements and guidance around the identification and determination of the components that are individually financially significant as this would lead to the most specific and comprehensive approach to the identification of such components. (See further decisions related to this in ED 2005 paragraph 8(c) and ED 2006 paragraph 14)
- (k) Develop application material on the types of work to be performed on significant components to ensure group audits are consistently performed in accordance with the ISAs.

#### Components that Are Not Significant Components

- (l) Add a requirement to require the group engagement team to vary the selection of components<sup>17</sup> that are not significant components over a period of time, and to restructure this sub-section, amending the requirements and expanding the application material around the performance of analytical procedures over these types of components. This was done to address concerns that some components may not be subject to audit procedures for a long period of time, and to respond to comments about additional guidance on the types of analytical procedures that could be performed and how they should be applied.

#### Obtaining an Understanding of the Component Auditor

- (m) Revise the requirement concerning the procedures to be performed in gaining an understanding of the component auditor (including restructuring and revising the related

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<sup>16</sup> Concern was raised that there may be jurisdictions where, due to legal or regulatory impediments, the group engagement team may not have access to relevant information, or the group engagement partner may be prohibited by law or regulation from refusing or resigning from an engagement.

<sup>17</sup> Including that the selection of components is often varied on a cyclical basis

application material), to address concerns raised around the nature, extent and documentation of the evidence obtained to demonstrate compliance with the ISA in this regard. (See further decisions related to this in ED 2003 paragraph 4(d) and ED 2005 (paragraph 8(e))

#### Involvement in the Work Performed by Component Auditors

- (n) Retain, but revise, the requirements for the group engagement team's involvement in the work of the component auditor (to make it more principles-based), and move to the application material examples of the types of group engagement team involvement. This was to address concerns about the prescriptive nature of the requirements and the fact that such requirements did not apply in all circumstances.

#### Communication with Component Auditors

- (o) Revise the communication requirements with the component auditor to allow for flexibility in the form of that communication, in recognition of the fact that communication may take place throughout the audit process in many different forms and, as such, may not always be in writing. All communications continued to be required to be on a timely basis, and certain matters were identified as required communications. (see also ED 2005, paragraph 8(e)(iv))

#### Responsibilities of Component Auditors

- (p) Require the group auditor to request that the component auditor confirm his/her cooperation with the group engagement team in respect of his/her work for the group audit, to address concerns that the proposed ISA should not contain explicit requirements for component auditors.

#### **Matter for IAASB Consideration**

- 2. Are there any other matters of significance relating to the development of the revised and redrafted ISA 600 that the IAASB believes are relevant to the background for the current group audits project?

### **C. Proposed Way Forward**

- 37. In addition to continuing to understand inspection findings, the IAASB is interested in the ongoing implementation of ISA 600 internationally, in particular to learn more about situations where ISA 600 is challenging to apply. Each group is structured differently and individual facts and circumstances will therefore impact how ISA 600 is applied by auditors. For example, groups may have differing degrees of centralization and commonality of systems and processes, so the very nature of the group and its environment results in the need for different applications of the standard. In some cases, what may look like similar facts and circumstances might be very different and might result in a very different audit approach. The world has also evolved since ISA 600 was revised and redrafted. Group structures are continually changing, for example, global companies are increasingly making use of shared service centers, for which ISA 402<sup>18</sup> and ISA 600 today provide only limited guidance.
- 38. Understanding whether ISA 600 is not only being consistently understood and applied as intended, but also whether it remains “fit for purpose” in a changing environment is essential. The Working

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<sup>18</sup> ISA 402, *Audit Considerations Relating to an Entity Using a Service Organization*

Group notes that the IAASB's recent experience has shown that obtaining appropriate information early in a project, in particular for purposes of scoping it, benefits projects in the long term. Obtaining input from interested stakeholders at an early stage is also expected to help further inform the IAASB as to the broad range of issues and potential actions to address them (e.g., whether standard-setting or other actions by the IAASB or others are appropriate or necessary) and appropriately focus the Board's efforts on the most significant issues.

*Development of a Discussion Paper*

39. As an initial step, the Working Group recommends that it develops a DP that outlines the issues identified, for the purposes of:

- Validating the issues that have been identified to date, requesting affirmation from respondents as to the appropriateness and completeness of the inventory of identified issues;
- Identifying any new issues, including evolving challenges in practice relating to applicability of ISA 600; and
- Soliciting feedback on the relative importance of the various issues and respondents' rationale for suggested prioritization.

It is proposed that the Working Group develop this DP with publication planned for after the September 2015 IAASB meeting.

40. As the Working Group develops the DP, it will also advise the IAASB as to its view whether roundtables or similar forums, using the DP as the basis for discussions, would be worthwhile. For example, it may be useful at the beginning of 2016 to engage interested stakeholders on specific identified issues where differing views have been identified (e.g., firm views, regulator views and NSS views). Doing so may help the stakeholders gain an understanding of others' views and may help stimulate discussions about an appropriate way forward.

41. In order to develop a robust DP, the Working Group intends to more thoroughly explore some of the identified issues through various interactions with relevant stakeholders. This will include understanding:

From Firms

- (a) Where additional implementation guidance has been developed to support effective and appropriately consistent implementation of the standard, in particular with respect to the application of tools assisting group auditors in their determination of the nature and extent of the involvement of the work of the component auditors, and how significant judgments about the nature and extent of involvement are documented.
- (b) The impact on the group audit if quality control procedures are implemented differently across networks.
- (c) Challenges in planning and performing group audits in an appropriately consistent manner (for example, what is being asked of component auditors may be different for firms in the same networks, and how component auditors execute against instructions, and how component auditors communicate with group auditors, may also differ).
- (d) How audit inspection findings and regulators' concerns are being addressed.

- (e) Challenges when firms within the same network conduct the group audit work; as well as challenges when firms other than those in the network are involved at the component level (including whether the challenges are more acute or new challenges arise).

From Regulators and Audit Inspection Bodies

- (a) The changing nature of inspection findings (for example, why the inspection focus may change).
- (b) Whether, and how, some of the findings in relation to ISA 600 have been addressed by the firms.

From All Stakeholders<sup>19</sup>

- (a) Cultural differences relating to the implementation and use of ISA 600 (for example, what may be culturally acceptable in one jurisdiction may not be so in another), as well as language and translation issues (e.g., such that once translated the implementation may not be performed in the same way as the original intention of the standard nor translated consistently in all languages).
- (b) Unique regulatory and legislative requirements which may also impact the way group audits are undertaken (for example, access to work papers).

For issues and concerns identified, the Working Group also intends to explore whether these are jurisdictional issues, or are globally applicable. This will help the IAASB understand what appropriate responses to the issues raised may be.

- 42. The feedback from the DP (and roundtables, if applicable) will be used as the basis for the project proposal, expected for Board consideration in June 2016. This will determine the standard-setting activities of the Board (or other activities as appropriate).

*Suggested Approach to Moving Forward*

- 43. The following sets out suggestions for the way forward to the expected project proposal:

<b>Timing</b>	<b>Outline of Working Group / IAASB Discussion</b>
March 2015 Consultative Advisory Group (CAG) meeting	Information session for the CAG about the issues relating to group audits (brief history, ISA Implementation Monitoring project findings, regulatory input, way forward)
March 2015 Board meeting	<ul style="list-style-type: none"> <li>(a) Information session for the Board about the issues relating to group audits (history, ISA Implementation Monitoring project findings, regulatory input)</li> <li>(b) Brief discussion on the way forward, including a discussion about further information gathering needed (as detailed in paragraph 41 above)</li> <li>(c) Letterbox audits – the way forward</li> </ul>

<sup>19</sup> The Working Group will also monitor the US Public Company Accounting Oversight Board's planned project proposal on "Supervision of Other Auditors and Multi-location Audit Engagements."

Timing	Outline of Working Group / IAASB Discussion
	(d) Outsourcing – information session about findings from firm survey
May 2015 NSS Liaison Group meeting	Discussion about some of the areas or further exploration discussed in paragraph 41 above.
June 2015 Board meeting	Further discussions about issues identified as a basis for the development of the DP
September 2015 CAG meeting	Draft DP for discussion, or relevant extracts thereof
September 2015 Board meeting	Draft DP for Board consideration (DP to be finalized by Working Group and released with a 90–120 day consultation period)
January – March 2016 (Timing would need to be confirmed)	Possible roundtables (or other format) to solicit additional input and feedback
March 2016 CAG meeting	Discuss feedback on DP
March 2016 IAASB Meeting	Discuss feedback on DP
June 2016 IAASB Meeting	Project Proposal for approval

**Matters for IAASB Consideration**

3. The IAASB is asked for its views on the way forward. Specifically, does the IAASB agree with:
- (a) The Working Group’s recommendation to develop a DP (with a decision about possible roundtables (or similar outreach) at a later point in time)?
  - (b) The proposed timing of the activities until the planned project proposal?
  - (c) The proposed topics / areas for further information gathering set out in paragraph 41 above? Are there any other areas the Board believe the Task Force should consider exploring as part of its information gathering activities or stakeholders whose views should be solicited in advance of the DP?

**D. Letterbox Audits – Proposed Way Forward**

44. The summary of the IAASB December 2014 Board discussions is included below.

**Decision Summary from the IAASB’s Discussions at Its December 2014 Meeting**

The Board recognized that the topic of letterbox audits has a long history and that the issue essentially relates to situations where there were concerns about the extent to which the financial statements had been sufficiently audited, and whether the person signing the opinion had been sufficiently involved in the audit engagement to be able to take responsibility for the audit and the related opinion. The Board was of the view that the question was not just whether ISA 600 applied to letterbox audits, but more broadly, an issue of audit quality in letterbox audit situations, including who should be signing the auditor’s report and whether such person had sufficient involvement in that audit to meet the

requirements in ISA 220.<sup>20</sup> A number of Board members noted that, although it may appear obvious that ISA 600 would apply to the letterbox audits in group situations, complex group structures exist which give rise to challenges in applying the definition of “group” as stated in ISA 600, such that the applicability of ISA 600 is not always clear in these situations.

In addition to thinking about the application of ISA 600 in group audit situations, Board members also highlighted the need to think more broadly about single component letterbox audits and whether and, if so, how ISA 600 might be adapted to address these situations, or how further clarification may be needed on how to apply the ISAs to these situations. The Board also noted that many of the challenges of applying ISA 600 to letterbox audit situations are also applicable to group audits generally.

The Board agreed with the Working Groups plans to gather further information about the challenges of applying the ISAs to letterbox audits from different stakeholders, how these challenges were being addressed, and specifically advised consulting audit firms and regulators, including IOSCO.

The Board also counseled the Working Group to consider the clarification of the application of the ISAs (including ISA 600 for group situations) to letterbox audits as a short term solution, possibly through an International Auditing Practice Notes (IAPN) or Staff guidance, but to also factor in the results of analysis of the related issues and implementation challenges into the broader project to revisit ISA 600.

#### *IAASB CAG Chairman’s Remarks*

Ms. de Beer noted that in practice some of the larger firms thought that ISA 600 did not apply to letterbox audits and it was important to understand why. She further noted comments made by the Board cautioning that ISA 600 should not be made to apply to letterbox audits if this was not the correct answer. Ms. de Beer suggested that there may be opportunity for a more immediate clarification of the application of ISA 600 and also noted that this could be a project that ultimately would affect many of the ISAs.

45. As part of its information gathering, the Working Group discussed certain regulator findings as detailed above (see “Regulatory Input and Audit Inspection Findings” in Section A above). Many of these findings were noted to be equally applicable to letterbox audit situations as to other group audit situations, however, a number of other issues were also identified that were specific to letterbox audits.
46. In particular, it was noted that group letterbox situations often involved large conglomerates, where it is not always clear who the group auditor is. Also, in these situations, there is often an intermediate holding company, the auditor of which often acts as a “pseudo” group auditor, issuing guidance to the component audit teams, and performing audit procedures on the consolidation.
47. In both the group and single component letterbox audit situations, it is understood that some firms believe that these situations are not contemplated or addressed by the ISAs and as such, there is no or insufficient guidance in the ISAs. Some firms therefore have developed their own guidance to address letterbox audits or certain types of letterbox audits. In practice, this can and has resulted in the auditor signing the opinion on the group or single component financial statements by relying solely on the opinion of the auditor of an intermediate company, component auditor or auditor of the single component in another jurisdiction – sometimes referred to as “back to back” opinions.

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<sup>20</sup> ISA 220, *Quality Control for an Audit of Financial Statements*

48. It is also understood that some firms are making amendments to their internal methodologies to update the interpretation of the ISAs with respect to letterbox audits, emphasizing the need to apply all relevant ISAs promoting a more consistent approach and eliminating practices that were not necessarily intended by the ISAs. However, the Working Group understands that this guidance may not, as of yet, be globally consistent, nor may it be consistently applied across global networks.
49. Based on this additional discussion and prior information gathering, it appears to be generally understood that ISA 600 applies to group audits in letterbox audit situations: however, there may not be consistent interpretation of when letterbox audits are group audits, and it also appears that there may be insufficient recognition that when applicable, ISA 600<sup>21</sup> builds upon the requirements of the other ISAs, including in particular, ISA 220.<sup>22</sup>
50. The Working Group therefore recommends a dual approach to addressing the challenges related to the topic of letterbox audits including a short-term response to clarify the application of the ISAs in letterbox audit situations (for both single and group letterbox audits, including ISA 600 in the case of letterbox audits that are also group audits) and a longer term response as part of the group audits project to address the underlying issues that are common to all group audits (i.e., including those that are letterbox audits).
51. As the short-term response, the Working Group recommends a brief Staff Audit Practice Alert or a brief Staff Q&A be issued to clarify that the auditor shall comply with all ISAs relevant to [an] audit<sup>23</sup> that is intended to be conducted in accordance with the ISAs, and in particular that ISA 220, which establishes requirements for direction, supervision and review of the audit, applies in all audits of financial statements, including for single component, as well as group, letterbox audit situations. It will also be made clear that, for letterbox audits that are group audits, the requirements of ISA 600 also apply and that these requirements build upon those in ISA 220. The Working Group is of the view that this publication would be responsive to the continued calls from some regulators and audit oversight bodies that the topic of letterbox audits be addressed on a priority basis.
52. The Working Group also recommends that as part of the longer-term response, the issues that are common to all types of group audits, including the extent of the involvement by the group auditor in the work of the component auditor, and any residual issues not addressed by the Staff publication, from part of the group audits project. In this way, the issues would be subject to additional information-gathering and other outreach activities to obtain further information about the implementation of ISA 600.
53. Additionally, as part of the longer term response, the Working Group will also liaise closely with the Quality Control Working Group, as some of the issues identified in this project may “cross-over” into that project, including as they pertain to single component letterbox audits.

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<sup>21</sup> ISA 600, paragraph 4, states, “In accordance with ISA 220, the group engagement partner is required to be satisfied that those performing the group audit engagement, including component auditors, collectively have the appropriate competence and capabilities. The group engagement partner is also responsible for the direction, supervision and performance of the group audit engagement.

<sup>22</sup> ISA 600, paragraph 5, states, “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 the component.

<sup>23</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraph 18

**Matters for IAASB Consideration**

4. Does the IAASB support the Working Group's recommendation for a dual approach to the topic of letterbox audits? Specifically:
  - (a) Does the IAASB support the issuance of a Staff document as a short-term action to address the challenges identified related to the application of the ISAs to letterbox audits?
  - (b) Does the IAASB support addressing the issues that are common to all group audits, including letterbox audits, as part of the larger group Audits project?

## Appendix 1

### Exposure Drafts Issued in Developing ISA 600 (Revised and Redrafted)

1. In finalizing the revised and redrafted ISA 600, the IAASB issued three ED's:
  - December 2003: Proposed ISA 600 (Revised), *The Work of Related Auditors and Other Auditors in the Audit of Group Financial Statements* (ED 2003) and International Auditing Practice Statement (IAPS),<sup>24</sup> *The Audit of Group Financial Statements*.
  - March 2005: Proposed ISA 600 (Revised), *The Audit of Group Financial Statements* (ED 2005).
  - March 2006: Proposed ISA 600 (Revised and Redrafted), *The Audit of Group Financial Statements* (ED 2006).
2. Set out below are the significant proposals from each ED.

#### ED 2003

3. The IAASB initially agreed that this would best be achieved by revising the existing ISA 600, *Using the Work of Another Auditor*, and developing a new IAPS on *The Audit of Group Financial Statements*. The proposed revised ISA 600 dealt with both “sole responsibility” and “division of responsibility,” and the proposed IAPS would apply when the group auditor took sole responsibility for the auditor’s report on the group financial statements.
4. Fundamental changes made in the initial drafts were to introduce the audit risk model into group audits,<sup>25</sup> and to make changes to require more involvement of the group engagement partner and group engagement team in the audit of group entities. Significant proposals in ED 2003 included:
  - (a) Changing the focus of ISA 600—widening the scope to require the “group auditor”<sup>26</sup> to determine how the work of the other auditors would affect the audit of group financial statements.
  - (b) Requiring more work for the group auditor at the acceptance and continuance stage, including obtaining a preliminary understanding of the group auditor’s ability to participate appropriately in the work of the other auditor, and therefore emphasizing the group auditor’s responsibility for the group audit.

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<sup>24</sup> IAPSs were issued to provide interpretive guidance and practical assistance to professional accountants in implementing ISAs and to promote good practice. Professional accountants are required to be aware of and consider IAPSs applicable to the engagement. A professional accountant who does not consider and apply the guidance included in a relevant IAPS is required to be prepared to explain how the standards and guidance in the ISA(s) addressed by the IAPS have been complied with. IAPSs were discontinued when IAPNs were introduced.

<sup>25</sup> ISA 600, paragraph 6 was introduced and further explained that audit risk in a group audit includes the risk that a component auditor may not detect a misstatement in the financial information in the component that may cause a risk of material misstatement in the group financial statements and the risk that the group auditor may not detect that misstatement (this paragraph is still in the extant standard). It goes on to explain that the group engagement team uses ISA 600 to determine the nature, timing and extent of risk assessment procedures and further audit procedures on the component to mitigate these risks.

<sup>26</sup> This term was changed to “auditor of group financial statements” in ED 2006.

- (c) More consideration about the group auditor’s access to information, such as access to component information, component management or other related auditors, and including consideration by the group auditor of the impact of any scope limitation arising therefrom.
  - (d) More consideration about the quality control processes of the other auditor (including the other auditor’s professional qualifications, independence, professional competence and resources).
  - (e) New requirements for “sole responsibility” for the group audit opinion. However, after extensive deliberations, the IAASB agreed to still allow “division of responsibility” in certain circumstances to help with practical implications expected when implementing the new requirements in certain jurisdictions.
  - (f) Separating related auditors from other auditors.
  - (g) A new proposed IAPS, including guidance on how to apply the (then) recently introduced audit risk model to group financial statement audits. The new IAPS suggested that it would be unusual for the group auditor to accept an engagement to audit group financial statements where the group auditor did not directly perform work on more than 50% of the group assets, liabilities, cash flows, profit, or turnover, unless able to participate appropriately in the work of the other auditor.
5. There was support for the project and acknowledgement that the proposed standard and guidance filled an important gap in the existing ISAs. However, many respondents had the view that the auditor’s responsibilities needed to be further strengthened and clarified. Due to the significance of the comments received to ED 2003, and the changes proposed to address the concerns and issues raised, the IAASB agreed that it was necessary to re-expose the revised standard and guidance.

#### *ED 2005*

6. The guidance from the proposed IAPS was moved into ED 2005 to respond to the view of the majority of respondents that this would avoid any confusion, minimize inconsistencies, eliminate repetition and lead to a shorter, more user friendly document that appropriately elevates the guidance contained in the IAPS and promotes consistency of application.
7. The option to divide responsibility for audits of group financial statements was removed.<sup>27</sup> The IAASB agreed that the group auditor should be responsible for issuing an audit opinion on group financial statements and, in order to obtain sufficient appropriate audit evidence on which to base that audit opinion, the group auditor should determine the audit procedures to be performed on the consolidation and other necessary work on the component’s financial information, regardless of who is performing the work.<sup>28</sup>

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<sup>27</sup> In the United States, an option under the standards of the American Institute of Certified Public Accountants and the Public Company Accounting Oversight Board today still allow the group auditor, in limited specified circumstances, the option to state in the auditor’s report that they have relied on the report of another auditor in reporting on the group financial statements, as well as indicating the name of another auditor on which they have relied. However, the group auditor still takes responsibility for the group audit opinion.

<sup>28</sup> The group auditor is responsible for expressing the group audit opinion, and therefore the group engagement team’s procedures are the same whether the group engagement partner accepts full or divided responsibility

8. Other significant changes on re-exposure included:
- (a) The requirement to consider the effect on the audit opinion if the group auditor is unable to obtain sufficient appropriate audit evidence in relation to a component<sup>29</sup> was added. The group auditor would no longer be able to refer to the other auditor, but would rather need to modify the audit opinion based on a scope limitation.
  - (b) The concepts of “related” (i.e., related to the group auditor)<sup>30</sup> and “other” auditors (i.e., not related to the group auditor), as included in ED 2003, were retained. The differences in the nature, timing and extent of procedures performed in relation to a related or other auditor’s work was also retained, but with procedures in relation to the “other auditors” being strengthened because respondents to ED 2003 had asked that the IAASB further consider the distinction in the audit procedures in relation to each. In this ED, the concept of an “unrelated” auditor (i.e., an auditor other than the group auditor or a related auditor who performs work on one or more components for the purposes of the audit of the group financial statements) was also introduced, with the distinction between related and unrelated auditors affecting the approach taken by the group auditor in relation to their work.
  - (c) ED 2005 provided more focus in ISA 600 on the involvement of the group auditor, particularly in relation to “significant components” (i.e., those likely to include significant risks to the group and those of “individual financial significance”<sup>31</sup>) including related guidance for identifying these components. The ED also introduced components that were “significant”,<sup>32</sup> those that were significant in aggregate, and those that were not significant in aggregate.<sup>33</sup>
  - (d) There was agreement that a restriction on the group’s auditors’ access (including to TCWG of the component, component management, component information or the other auditors) is a scope limitation that the group auditor would need to consider when forming the opinion.

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<sup>29</sup> See ISA 600, para 45

<sup>30</sup> There was the view that network firms would have common quality procedures across networks, and therefore the involvement of the group auditor could be less to acknowledge these common quality control procedures. There were, however, concerns, in particular by some regulators, whether the network firms did have the same levels of quality control, notwithstanding that they may be “common.” In particular, there were concerns that there are factors other than common quality control policies and procedures that need to be taken into account. In addition, smaller firms who were unable to benefit from such common quality control policies and procedures had the view that they were at a disadvantage in performing work on group audits even though the group auditor may be intimately familiar with the component auditors and their work, and is satisfied with that work.

<sup>31</sup> Paragraph 16 of ED 2005 noted that “Generally, a relatively small number of components will constitute a large portion of the group’s operations and financial position, making them financially significant. The group auditor may apply a percentage to a chosen benchmark as an aid to identify components that are of individual financial significance. Although in practice there are ranges of possible percentages, a component representing 20% or more of group assets, liabilities, cash flows, profit or turnover is regarded as financially significant.”

<sup>32</sup> ED 2005 defined “significant components” as a component that has been identified at the group level as likely to include significant risks of material misstatement of the group financial statements. This could be due to (i) the nature of, and circumstances specific to component (risk), or (ii) the individual financial significance of the component to the group (size).

<sup>33</sup> Paragraph 54 of ED 2005 noted that “While in practice there are ranges of possible percentages, components that in aggregate represent less than 5% of group assets, liabilities, cash flows, profit or turnover will ordinarily be regarded as not significant in aggregate.”

- (e) The requirements relating to the group auditor’s work effort were strengthened, including the:
- (i). Determination of the type of work to be performed on the component’s financial information.
  - (ii). Involvement in the work of the other auditors.
  - (iii). Evaluation of the adequacy of the other auditors’ work.
  - (iv). Communications with the other auditors.

*ED 2006*

9. Based on the comments received to ED 2005, the IAASB made further changes to the proposed standard, and redrafted the text to reflect the proposed clarity drafting conventions, issuing ED 2006 in March of that year. The significant issues raised by respondents, and the IAASB’s response, are discussed below.

<b>Respondents’ Comments</b>	<b>IAASB Response</b>
10. A majority of respondents to ED 2005 supported the elimination of the distinction between sole and divided responsibility.	In ED 2006, the IAASB confirmed its previous conclusion that the group auditor is responsible for the group audit opinion, and has to perform procedures to obtain sufficient appropriate audit evidence to reduce audit risk for the group financial statements to an acceptably low level.
11. Respondents to ED 2005 were concerned about the consistent application of the proposals relating to “related” and “unrelated” auditors. Several respondents also asked the IAASB to clarify the group auditor’s proposed involvement in the work of another auditor (including the review of the other auditor’s audit documentation).	The IAASB acknowledged that the structures of audit firms and audit firm networks varied and that it would not be possible to develop a distinction between related and unrelated auditors that would be consistently applied in all cases. The IAASB therefore eliminated the distinction and revised the guidance to explain the effect of audit risk of using the work of another auditor. <sup>34</sup> The IAASB also revised the requirement to base the group auditor’s decision whether to review relevant parts of another auditor’s audit documentation on his or her evaluation of the other auditor’s memorandum or report of work performed.

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<sup>34</sup> This acknowledged that firms and other engagement circumstances were not the same and that a principles-based approach using a sliding scale based on the relevant circumstances would be the most appropriate approach (see in particular ISA 600 paragraph 19 in connection with paragraphs A33–A36, and paragraphs 25 and 30–31 in connection with paragraphs A47 and A54–A55. The IAASB rejected detailed requirements covering different kinds of circumstances because the circumstances vary widely and therefore considerable auditor judgment needs to be exercised).

<b>Respondents' Comments</b>	<b>IAASB Response</b>
<p>12. The majority of respondents supported the new material on the group auditor's decision to accept or continue an engagement (i.e., subject to the group auditor being able to obtain sufficient appropriate audit evidence on which to base the group audit opinion, by the group auditor performing work on significant components, or being involved in the work of other auditors performing work on significant components). However, concern was expressed about the percentages being applied to a benchmark<sup>35</sup> to determine "significant components".</p>	<p>The IAASB continued to have the view that this guidance was useful, but rearticulated it to be less prescriptive and rather included in the application material. The concept of using a benchmark against assets, liabilities, cash flows, profit or turnover was retained, however, the benchmark suggested was decreased from 20% to 15% of the chosen benchmark.</p>
<p>13. Concern continued to be expressed about issues related to the revised requirements about the group auditor's access to component information and management / TCWG. In particular, it was noted that there should be more guidance on what the group auditor should do if there were restrictions on access.</p>	<p>Although recognizing that these circumstances exist, the IAASB continued to have the view that if the group auditor was unable to be involved in the work of another auditor, it would be unlikely that the group auditor would be able to obtain sufficient appropriate audit evidence on which to base the opinion, and accordingly the group auditor should refuse or resign from the engagement.</p>
<p>14. Respondents to ED 2005 found it difficult to distinguish between components that were "significant in aggregate" and "those that were not significant in aggregate."</p>	<p>To eliminate any confusion, the IAASB combined these categories as "components that are not individually significant" (with relevant guidance on how to identify these) and specified audit procedures in relation to these. For any other components not selected, the IAASB required the group auditor to perform analytical procedures at the group level. The IAASB also added guidance to make the determination, and the work to be performed on these components.</p>
<p>15. Some respondents had noted that it was not clear whether an auditor from another office of the group engagement partner's firm is a member of the group engagement partner's engagement team or a related auditor.</p>	<p>The IAASB defined the group engagement team as partners, including the group engagement partner [separately defined], and staff who establish the overall group audit strategy, communicate with component</p>

<sup>35</sup> The proposed guidance recognized that the group auditor may apply a percentage to a chosen benchmark as an aid to identify components that were of individual significance. It also explained that a component representing more than 20% or more of group assets, liabilities, cash flows, profit or turnover was regarded as financially significant.

Respondents' Comments	IAASB Response
	auditors, perform work on the consolidation process, and evaluate the conclusions drawn from the audit evidence as the basis for forming the opinion on the group financial statements.

16. In addition, notwithstanding that the extant standard at that time included a requirement for the component auditor to cooperate with the group auditor (based on understanding the context in which the group auditor will use the other auditor's work), the IAASB did not consider it appropriate to include any requirements for another auditor in an ISA that primarily contains requirements and guidance for the group auditor. The IAASB did, however, agree to include a requirement for the group engagement team to obtain the component auditor's confirmation on such cooperation.
17. The IAASB also continued to maintain the requirements and guidance relating to group audits in one ISA (and not revert back to an ISA and an IAPS as originally proposed in ED 2003). In addition, the final standard exposed was redrafted in the Clarity format, with some application material being moved to appendices.