

1 October 2020

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International Auditing and Assurance Standards Board
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Dear Sir,

RESPONSE TO THE INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD (IAASB) EXPOSURE DRAFT (ED) ON PROPOSED INTERNATIONAL STANDARD ON AUDITING 600 (REVISED)

The Institute of Singapore Chartered Accountants (ISCA) appreciates the opportunity to comment on the above ED issued by the IAASB in April 2020.

To solicit meaningful feedback for the topic, ISCA undertook the following initiatives to seek views from key stakeholders:

- (i) Conducted targeted public consultation to seek feedback from members
- (ii) Solicited feedback on the ED from members of the ISCA Auditing and Assurance Standards Committee.

Our comments to selected questions in the ED are as follows:

ISA 600 (Revised) Specific Questions

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

We support the definition of group financial statements under paragraph 9(k), including the linkage to a consolidation process, as the purpose of a group audit is to provide a basis for forming an opinion on consolidated financial statements which are outputs of a consolidation process as described under IFRS 10 *Consolidated Financial Statements*.

We welcome the clarification on the applicability of the standard to branches or divisions set out under paragraph A17 which explains that the standard does not apply to situations where there is no separately prepared financial information for the branches or divisions that require aggregation.

Regarding the removal of paragraph 2 in the extant standard which relates to application by analogy to a situation that is technically not an audit of group financial statements, but where there are similarities and the principles in this standard may be useful, we suggest to reintroduce this paragraph or include additional material regarding situations involving other auditors in the audit of financial statements that are not group financial statements.

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

We support the revised definition of a component under paragraph 9(b) to focus on the auditor’s perspective, as this provides greater flexibility for group auditors to decide how the audit should be best executed from a risk and efficiency standpoint instead of being confined to the concept of legal entities. This is especially useful for groups that may organise themselves by function, process, product or service etc. It could also allow for better focus on identifying, assessing and responding to the risks of material misstatement.

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

The inclusion of guidance regarding restrictions on access to people and information that are beyond the control of group management is helpful as it drives group auditors to better consider this upfront at the audit acceptance and continuance stage and in early planning.

However, we have some specific concerns as follows:

(i) Restriction of access to non-controlled entities

We appreciate the IAASB’s recognition of this issue and the guidance provided in paragraph A29 of the ED to overcome restrictions to entities which are not controlled by the group (such as those accounted for by the equity method).

This is an area which might attract complications where the non-controlled entity limits the level of access to information and/or its auditors.

While we find the guidance provided in paragraph A29 to be useful, we also wonder if this might give the wrong impression to the group management or non-controlled entities that the group engagement team could just make do by carrying out some of the suggested procedures, such as considering publicly available information. This might lead to situations where the group engagement team is pressured to “deal with it” as the standards appears to allow it.

It would be helpful to emphasise that these procedures suggested are meant for consideration only and, by themselves, might not be sufficient to overcome the restriction.

(ii) Practical challenges in reviewing component auditor documentation remotely

Against the backdrop of Covid-19, the issue of restrictions to access to information has become more apparent, particularly where the source audit documentation is not allowed to be shared outside the jurisdiction due to laws and regulations.

As listed in paragraph A29, some of the methods by which group engagement teams (GETs) overcome such restriction is by reviewing the component auditor’s working papers remotely through the use of technology, such as via video conferencing or by discussing procedures performed with the component auditor. While these are workable alternatives, there are accompanying risks and challenges, for instance the reliability of the evidence obtained through such means and the level of cooperation required from the component auditors.

In this regard, we hope that the application materials can instil awareness on the risks arising from using technology and provide guidance on considerations before the GET can rely on the audit evidence obtained through such means to ensure that the quality of audit evidence is not compromised.

It may be helpful for GETs if there are considerations or application guidance in the standards in relation to matters affecting acceptance and continuance that are not within management’s control, for example in situation where component is located in a country where the regulatory environment is not robust.

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

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

(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?

Responsibilities of GET and component auditors

We believe that the recognition of the need to involve component auditors to identify and assess risks of material misstatement at the component level is consistent with the principles of ISA 315 (Revised). While we support the concept of involving the component auditors at this phase of the audit, this needs to be balanced with an independent assessment by the GET as there may be conflict of interest on the component auditor's part to have reduced involvement. This is particularly important in situations where the component auditors may be performing the procedures only for the purpose of group reporting and are not signing off on the standalone financial statements of the component or where group reporting requires additional work on top of their statutory audit.

In this regard, we believe that the emphasis on the GET's responsibilities throughout the ED, such as under paragraphs 31 and 33, are sufficiently clear.

However, we are concerned that the revised approach to risk identification and assessment, which requires the group auditor to take a "top-down" and more "horizontal" view of the group audit overall, with very granular upfront involvement, is likely to be challenging. Below are our views on some of the practical challenges.

Interactions between the group engagement team and component auditors

De-emphasis of an audit of the component financial information

We are concerned, in particular, that an audit of the component financial information as an appropriate response in the context of a group audit appears to be de-emphasised within the ED and addressed only in the application material, or in respect of using an audit already performed over a component for statutory or other purposes.

We noted that the usage of the term "audit" is not used and instead, replaced with terminology such as obtaining evidence over "the entire financial information of the component", without further elaboration. The aim of driving greater direction and supervision of the group audit as a whole by the group engagement partner has resulted in a de-emphasis of a full-scope audit of component financial information.

In this regard, we believe that it may be appropriate, or even necessary, in certain situations to require the component auditor to perform an audit over the component financial information. We suggest that the application material expands on the current content in relation to the following areas.

When to involve a component auditor

We recommend that the standard provide further clarity on when it would be appropriate or optimal to involve a component auditor, including greater acknowledgement that using the work of a component auditor may result in a more effective approach to obtaining sufficient appropriate audit evidence.

How to involve a component auditor

There is very little direction as to the procedures component auditors would be requested to perform as the most appropriate response to the risks identified. We recommend that the standard describe within the application material the different ways to involve a component auditor in terms of the nature, timing and extent of their involvement in performing procedures in the context of obtaining evidence over “the entire financial information of the component” and provide a framework, including factors and thresholds that the group engagement team would consider in making the determination as to how to involve a component auditor.

Iterative nature of involvement of component auditors

Under the current model in the extant ISA 600 of identifying significant components based on financial significance, the component auditor is expected to report on any risks that is above the assigned materiality. This would include identification and addressing risks arising after group audit instructions are sent out by the GET. The component auditor would also be expected to inform (or pre-warn) the group auditors of such risks. This would be helpful for the GET given that risk identification is an iterative process throughout the whole audit.

However, under the new risk-based approach where the GET only involves component auditors for risks identified, there seems to be an apparent intention for a more “piecemeal” involvement of the component auditors, with the de-emphasis on performance of a full scope audit over component financial information.

The application material, in describing the work that a component auditor may be requested to perform, appears to “divide” this into risk assessment procedures, including developing an initial expectation, and performing further audit procedures assigned by the group engagement team in response to those risks (paragraph A97). This may be challenging to operationalise in practice, especially for larger and more complex groups, putting significant pressures on reporting timetables, which may even be impracticable to be executed in certain cases. In a situation where the component auditor is from another network, it would be even more difficult to work in such close coordination and in an iterative fashion, as intended by the ED. It is therefore vital that component auditors have clearly defined role and responsibilities in this area, given the importance of their contribution to the group audit. As recommended above, the standard should be enhanced to provide a clear framework to GETs regarding when and how to involve component auditors.

Two-way communication

The proposed standard emphasises the importance of two-way communication between GETs and component auditors throughout the audit, for example, under paragraph 43, in terms of the audit as a whole, and elsewhere in relation to specific aspects of their involvement. We recommend that expectations over communication by the component auditors be strengthened to complement these paragraphs.

Practical challenges

While we support the rationale of adopting a risk-based approach, we foresee the following challenges:

If the assessed risk is not aligned by legal entities or business units, it may not be straightforward to coordinate audit efforts across the group and this would need the support and involvement of group management. GETs may face difficulty communicating the benefits of this revised approach to group management who are used to the existing approach of segregating the components by legal entities or business units.

The risk-based approach may be challenging to implement, especially for large and complex groups with many heterogenous components. As mentioned above, a group audit is a highly iterative process and the scope of work can develop gradually and continue to evolve as the audit progresses, resulting in practical difficulties for GETs to provide clear, upfront instructions to component auditors regarding the intended nature, timing and extent of their involvement in the group audit. There could be a possibility that new risks arising in those components might not be identified until a later stage. When the GET identify such risks during the consolidation stage, the GET will need to request for the component auditor to perform additional procedures, creating significant pressures on reporting timelines. This might not be a feasible approach for audits of publicly listed groups which have tight timelines. To avoid this risk, GETs might revert to the existing approach of requiring component auditors to report on all areas based on the assigned materiality. Also, as mentioned above, if the component auditor is not from the same network, it may not be possible to implement such close and continuous liaison to implement the new approach may not be practical.

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

In setting component materiality, the benchmark that is used (such as group assets, revenue or profit, etc) may differ between components depending on their function or nature of activities. However, it is sometimes observed that this is not considered by GETs and a consistent benchmark is applied across all components, resulting in the component materiality set not cognizant with the risk of the component. It may be worthwhile to highlight this under A75 of the application material.

We are also of the view that the requirements in regard to aggregation risk is not sufficiently clear in the application material, in particular paragraph A11. It would be quite difficult for practitioners to understand and apply the concept in practice based on the broad principles-based guidance in the ED.

We are aware that some firms are using models such as the Maximum Aggregate Component Materiality (MACM) to perform a high-level reasonableness check. More

practical guidance would be required in this area for practitioners to properly address this risk.

We suggest for the standard to include a requirement to communicate, or consider the need to communicate, component materiality when the component auditor is requested to perform:

- An audit of component financial information; or
- An audit of an account balance, significant class of transaction, or disclosure

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

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

(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?

We welcome the enhancements to the documentation requirements to emphasise the linkage to ISA 230 *Audit Documentation*.

Paragraph A124 states that audit documentation may reside in the component auditor's file and need not be replicated in the GET's audit file. However, the paragraph further notes that the GET may determine that it is appropriate to include certain of the component auditor's documentation in the GET's audit file, the extent to which is determined by the GET.

For consistency in practice, we recommend providing factors to consider in determining whether and what part of the component auditor's documentation should be included in the GET's audit file in the application material. Otherwise, it would be helpful to clarify whether the "original" component auditor documentation (source working papers), or documentation that is similarly detailed, should generally be included in the GET's file, with evidence that the GET has reviewed such documentation, or a more summarised form of component auditors' documentation, which primarily focuses on actions taken by the GET to understand significant risks and audit procedures performed in response to those risks, would be sufficient.

We welcome the inclusion of guidance under paragraphs A129 and A130 to address circumstances when laws and regulations in the component auditors' jurisdictions may limit the ability of the group engagement team to access the component auditor's documentation.

We consider it helpful that the application material includes guidance that the GET's audit documentation may need to include a description of the audit procedures performed by the component auditor on matters relevant to the group audit, the evidence obtained and the findings and conclusions reached. Similar to our point above, it would be helpful to clarify whether a memorandum from the component auditor providing summarised details of the

work performed and related findings would be appropriate, or whether the detailed test work itself would need to be included.

To this end, we suggest that further clarity could be provided as to what constitutes group audit documentation and where this should reside.

To provide practical guidance, we are of the view that the application material can be further expanded to provide illustrative examples over the following areas:

- Examples of what would clearly constitute insufficient documentation.
- Example of supplementation documentation where it is not apparent from the reporting deliverables that significant risks of misstatements have been addressed.
- Example of documenting communication with component auditor to be retained as audit evidence.
- Example of documenting GET's assessment of the component auditor's work

We would like to share an audit practice bulletin issued by our regulator in December 2015 – Audit Practice Bulletin No. 1 of 2015: Audits of Group Financial Statements (including the work of component auditors) which includes illustrative examples on GET's audit documentation for the IAASB's reference.

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

Paragraph 45(b) states that the GET shall determine whether, and the extent to which, it is necessary to review parts of the component auditor's audit documentation.

We find that there is an expectation gap amongst the stakeholders on whether it is always necessary to review the component auditor's audit documentation. While paragraph 45 (b) and paragraph A113 of the ED seem to suggest that this depends on the GET's judgement, GETs find it a challenge to defend a decision of not reviewing a component auditor's audit documentation solely based on this guidance (paragraph A113 of the ED).

If it is not an expectation that it is always necessary for GETs to review parts of the component auditor's audit documentation, perhaps the inclusion of such a statement in the standard would provide clarity on this matter. However, emphasis that the GETs need to properly document the basis for arriving at such a conclusion should be included.

Should you require any further clarification, please feel free to contact Ms Wang Zhumei, Manager, Technical: Audit & Assurance, at ISCA via email at zhumei.wang@isca.org.sg

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Ju May', with a stylized flourish at the end.

Ms Ju May, Lim
Deputy Director
TECHNICAL: Financial & Corporate Reporting;
Ethics & Specialised Industries;
Audit & Assurance