



June 21, 2022

Ms. Sherry Hazel
Audit and Attest Standards
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

RE: Proposed Statement on Auditing Standards, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Auditors)*

Dear Ms. Hazel:

We appreciate the opportunity to comment on the Proposed Statement on Auditing Standards, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Auditors)* (the proposed SAS). Overall, we support the intent of the proposed revisions to AU-C section 600.

We support the Auditing Standards Board's (ASB) strategic objective of convergence with International Standard on Auditing (ISA) 600 (Revised)¹ of the International Auditing and Assurance Standards Board (IAASB). We commend the ASB for enhancing its processes to provide more timely feedback into the IAASB's standard-setting projects and taking prompt action to expose the proposed SAS shortly following the IAASB's finalization of ISA 600 (Revised).

We believe it is important that the proposed SAS supports auditors in being able to scope and plan the audit as is most appropriate to the nature and circumstances of the group, and recognizes the important roles both group and component auditors play in contributing to group audit quality. In this regard, it is important that, in moving away from some well-recognized concepts in extant AU-C section 600 (e.g., significant components), the ASB is satisfied that the proposed SAS continues to support high-quality group audits, including consistent judgments about scoping of the group audit and the nature, timing, and extent of the involvement of component auditors.

The following overall observations are described in more detail in Appendix 1 in response to the specific questions posed in the exposure draft.

Alignment with PCAOB proposals

We believe the ASB should evaluate the forthcoming Public Company Accounting Oversight Board (PCAOB) proposed final amendments relating to the planning and supervision of audits involving other auditors.² Audit firms that audit large multinational companies may need to have policies and procedures in place that comply with the IAASB, PCAOB, and ASB standards, and therefore we strongly encourage alignment between the standards issued by these standard-setting bodies when appropriate. We suggest the ASB staff analyze the final PCAOB standard and any amendments to other standards and consider whether changes to requirements or guidance in the proposed SAS may be helpful to drive more consistency in group audits performed in the US.

Specifically, we note that the PCAOB has proposed revisions related to the use of referred-to auditors, which is a concept that does not exist under the IAASB's ISAs, but that has been retained by the ASB in

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

² On June 14, the PCAOB announced an open meeting to consider adoption of new requirements for the lead auditor's use of other auditors.



the proposed SAS. As drafted, the requirements related to referred-to auditors in the proposed SAS have been drafted based on extant requirements, with additional requirements added to mirror the requirements when component auditors are involved. These new requirements appear to be more restrictive than the requirements proposed by the PCAOB when dealing with referred-to auditors; we question if the incremental work effort required by the proposed SAS is necessary for non-public companies audited under ASB standards as compared to public companies audited under PCAOB standards. Because the concept of referred-to auditors is unique to the US environment, we encourage the ASB to seek closer alignment with the PCAOB.

Interaction with quality management standards

It is important that the requirements in the proposed SAS are clear insofar as how they interact with requirements in the newly approved quality management standards, particularly SAS 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards* and the new Statement on Quality Management Standards (SQMS) 1, *A Firm's System of Quality Management*.

As described further in our response to question 1 in Appendix 1, the proposed SAS generally appears to strike an appropriate balance between the responsibilities of the group engagement team and component auditors. However, we encourage the ASB to monitor questions and issue additional guidance, if necessary, that describes how the requirements in SAS 146 are to be applied in a group audit should questions arise as the proposed SAS is implemented. The ASB should also seek feedback from the Peer Review Board and others to understand whether the proposed SAS and SAS 146 are achieving their intended objectives.

Engagement with the Professional Ethics Executive Committee (PEEC)

As described further in our response to question 1 in Appendix 1, we believe it is urgent for the PEEC to determine and conclude on whether there are implications to the AICPA's Code of Professional Conduct as a result of the International Ethics Standards Board for Accountants' project to align the definition of the term "engagement team" with the IAASB's definition and establish provisions that comprehensively address independence considerations for firms involved in a group audit. A coordinated approach between the ASB and PEEC to consider their respective standards and guidance that is finalized before SAS 146 and the proposed SAS become effective is essential.

Effective date

We appreciate that the ASB has aligned the proposed effective date of the proposed SAS with the effective date of SAS 146.

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We provide further context to the above points in our responses to the ASB's detailed questions in Appendix 1, and offer drafting suggestions in relation to the proposed SAS in Appendix 2.

We appreciate the opportunity to express our views and would be pleased to discuss our comments or answer any questions you may have. Please contact Heidi Schuetze at heidi.schuetze@pwc.com or Kathleen Healy at kathleen.k.healy@pwc.com regarding our submission.

Sincerely,

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP



Appendix 1 - Responses to specific questions

1. With respect to the linkages to other AU-C sections
 - a. does the proposed SAS have appropriate linkages to other AU-C sections and to the proposed SQMSs?
 - b. does the proposed SAS sufficiently address the special considerations in a group audit as they relate to applying the requirements and application material in other relevant AU-C sections, including the proposed QM SAS? Are there other special considerations for a group audit that you believe have not been addressed in the proposed SAS?
 - c. does the proposed SAS result in a group audit that achieves the objectives of the proposed QM SAS?

With regard to question 1.a., we generally believe the proposed SAS has appropriate linkages to other AU-C sections and to the SQMSs. However, with regard to questions 1.b. and 1.c., there are some areas that could be further clarified within the proposed SAS, and additional special considerations in a group audit that the ASB could explore, to ensure the proposed SAS achieves the ASB's objectives in revising it as well as the objectives of SAS 146. Appendix 2 includes drafting suggestions to complement our responses below.

Linkage to SAS 145 / AU-C section 315 (Revised)

We support the enhanced focus expressed in paragraph 32 of the proposed SAS to understand the group and its environment. The structure of a group and its financial reporting processes and controls play a significant role in determining how best to approach a group audit, the key judgments that need to be made around the determination of components, and how component auditors are involved in the audit. Such judgments need to be based on a preliminary understanding of how management views and controls the business, taking into account the group, its structure, its financial reporting processes, and system of internal control. Different approaches may be justified depending on the group's structure and circumstances.

We understand the benefit of enhanced focus on describing how component auditors may support the identification and assessment of risks of material misstatement of the group financial statements, and the design of procedures to respond to those assessed risks. However, the proposed SAS should not be read as suggesting that it is always necessary to involve component auditors in this manner (e.g., the group auditor may choose not to involve the component auditor in the risk assessment when the work at the component comprises only "specific further audit procedures"). We suggest edits in Appendix 2 to balance the discussion about involving component auditors in all phases of the audit, including risk assessment.

Linkage to SAS 146 / AU-C section 220 (Revised), including achievement of its objectives

It is important that the requirements in the proposed SAS are clear insofar as how they interact with requirements in the newly approved quality management standards, particularly SAS 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards* (referred to in the question as the QM SAS) and the new Statement on Quality Management Standards (SQMS) 1, *A Firm's System of Quality Management*. In our view, the application material in the proposed SAS is helpful to understand how the requirements in both SAS 146 and the proposed SAS are to be applied in the context of group audits. However, due to the complexities that may exist in a group audit, it is likely questions will arise during the implementation of SAS 146 and the proposed SAS, in particular with respect to direction, supervision and review of the work of component auditors. We encourage the ASB to monitor questions and issue additional guidance, if necessary, about how the requirements in SAS 146 would be applied in a group audit. After the proposed SAS is implemented, the ASB should seek feedback from the Peer Review Board and others to understand whether the proposed SAS and SAS 146 are achieving their intended objectives.



As we noted in our response to the exposure draft of the proposed quality management standards, today's audits are being performed with increasingly diverse and distributed delivery models that leverage technology, other tools, and working practices to increase the effectiveness and efficiency of audit work. As entities and audits become more distributed, it is often necessary to involve others, such as component auditors, to assist the engagement partner in directing, supervising, and reviewing the engagement.

Effective interaction between the group auditor and component auditors is important to audit quality, and we agree that the engagement partner needs to be sufficiently and appropriately involved throughout the audit to be able to take overall responsibility for the quality of the group audit engagement. However, we think it important that there be shared accountability for quality when firms use component auditors.

We agree with the following points highlighted in SAS 146:

- AU-C section 600 provides guidance on how to adapt and apply the requirements of SAS 146 in an audit of group financial statements involving component auditors.
- When others such as component auditors perform supervisory and review activities, the outcomes of those activities can be taken into account by the engagement partner in fulfilling their responsibilities in SAS 146. For example, the engagement partner may find it necessary to seek input from others with responsibilities for direction, supervision, and review to make determinations (i) about whether sufficient and appropriate resources are assigned or made available to the engagement team in a timely manner; and (ii) that members of the engagement team and others collectively have the appropriate competence and capabilities, including sufficient time, to perform the audit engagement.
- The group engagement partner exercises professional judgment when determining the nature and extent of the review of component auditor work in a group audit.

We also agree with retaining the US concept of dividing responsibility by making reference to another auditor's opinion on the audit of a component in the group auditor's report on the group financial statements. We agree it is helpful for the ASB to develop a new definition of a "referred to auditor" and to clarify that they are not considered a component auditor and therefore note part of the engagement team for a group audit.

The proposed SAS generally appears to result in a group audit that achieves the objectives of SAS 146, and strikes an appropriate balance between the responsibilities of the group engagement team and component auditors. However, we encourage the ASB to consider whether it is sufficiently clear that component auditors are responsible for the performance of their work in accordance with AICPA standards, in particular SAS 146.

Special considerations in a group audit

We generally believe the proposed SAS sufficiently addresses the special considerations in a group audit, with the exception of our views that follow on (i) changes to the definition of engagement team with respect to independence and ethics in a group audit; (ii) how the engagement partner can direct, supervise, and review the work of a component auditor that is not part of the same network as the group engagement team; and (iii) considerations relating to sharing audit evidence across the group audit.

Implications of changes to the definition of engagement team with respect to independence and ethics in a group audit

We believe the implications of the change in SAS 146 to include component auditors within the definition of engagement team are unclear, particularly in terms of compliance with independence and ethical



requirements. While group auditors and component auditors today communicate about breaches of independence requirements, the variety of ethical requirements that could apply in a group audit may present legal and other challenges that have not been fully considered (e.g., in relation to confidentiality and sharing of information). This is likely to be heightened when component auditors are not from within the same network as the group engagement team – such circumstances are increasing as a result of mandatory audit firm rotation in some jurisdictions.

We note that the International Ethics Standards Board for Accountants (IESBA) has a current project to align the definition of the term “engagement team” in its International Code of Ethics for Professional Accountants with the revised definition in ISA 220 (Revised),³ and establish provisions that comprehensively address independence considerations for firms and individuals involved in a group audit. We believe it is urgent for the PEEC to determine and conclude on whether there are implications to the AICPA’s Code of Professional Conduct as a result of the IESBA’s work and the changes to the definition of the engagement team in SAS 146. Changes to the AICPA Code of Professional Conduct could result in the need for additional guidance to enable auditors to consistently apply the requirements in the standards. A coordinated approach between the ASB and PEEC to consider their respective standards and guidance that is finalized before SAS 146 and the proposed SAS become effective will be essential.

Execution of responsibilities related to direction, supervision, and review when the component auditor is not part of the same network

It would be helpful to add additional application material to paragraph A81 to assist engagement partners in complying with paragraph 30 of the proposed SAS, which discussed the engagement partners’ responsibility for the nature, timing, and extent of direction, supervision, and review when component auditors are from non-network firms. While paragraphs A23-A24 of SAS 146 note that the engagement partner may need to take different actions when dealing with an individual from another firm, this application material is focused solely on understanding competence, capabilities, compliance with ethical requirements, and independence and not other aspects of SAS 146.

In principle, when a component auditor is not part of the same network, we would expect that efforts to understand matters such as the competence and capabilities of the component auditor would focus on inquiry, knowledge of and prior experience with the component auditor, and consideration of publicly-available information that might indicate concerns with the quality of the component auditor’s work (including communications regarding the component auditor’s professional competence from professional bodies, licensing authorities, or other third parties). Importantly, the nature and extent of these efforts will depend on how the component auditor is being used and the facts and circumstances of the engagement. Communications from the component auditor would also be taken into account. If based on this, the group auditor has concerns about the competence and capabilities of the component auditor, the planned involvement in the work of the component auditor would likely increase, or the group auditor might ultimately conclude it is inappropriate to use the component auditor.

To facilitate consistent application in practice when the component auditor is not part of the same network (and therefore may not be subject to the same policies and procedures), the ASB could consider developing application guidance that incorporates the following:

- At the commencement of the engagement, communication with the component auditor regarding their own responsibilities for direction, supervision, and review in accordance with SAS 146 and obtaining acknowledgement of compliance
- Throughout the audit, understanding the areas on which the engagement partner at the component has devoted attention

³ ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*



- Similar to paragraph 28 of the proposed SAS, considering whether publicly-available information about the results of the monitoring and remediation process or external inspections related to the component auditor indicate there may be specific concerns related to direction, supervision, and review

There may be other considerations that could be addressed when the group auditor and component auditor are not part of the same network and therefore do not have common systems of quality management, including in relation to the group auditor's consideration of the use of technological resources. This may be an area where non-authoritative guidance outside of the proposed SAS may be helpful to explain what may be appropriate in the circumstances.

Considerations relating to sharing audit evidence across the group

While the proposed SAS seeks to clarify the role of shared service centers, we believe this is an area that may continue to give rise to questions. Increasing centralization of accounting and reporting processes into shared service centers by group entities means that audit work related to those processes also needs to be performed on a centralized basis to obtain audit evidence that will be relevant to group audits, audit work at components, and stand-alone statutory audits. This has implications for component audits, including with regard to how they can use evidence obtained from testing at a shared service center (which is often performed by the group auditor or another component auditor). This circumstance is not considered in the ISAs or existing AICPA standards. We believe there is merit in the ASB considering whether the proposed SAS or a separate project could address how component auditors across the group are able to demonstrate that they have fulfilled their responsibilities in relation to evaluating the sufficiency and appropriateness of the shared evidence without duplicating effort.

Other matters

We encourage the ASB to consider whether it might be helpful to develop illustrative interoffice/interfirm reports, for inclusion either in the proposed SAS or as non-authoritative guidance to support the standard. Doing so may help build consistency in practice. Alternatively, this could be undertaken as part of a broader exercise to determine whether other examples of how firms in the US may be requested to communicate with each other (e.g., in the case of predecessor/successor auditors) would be helpful to auditors.

2. With respect to the structure of the proposed SAS, do you support the placement of subsections throughout the proposed SAS that highlight the requirements when component auditors are involved or when reference is made to the audit of a referred-to auditor in the auditor's report on the group financial statements?

Yes, the sub-sections in each section of the standard clearly set out considerations for the group engagement team when component auditors are to be involved in the group audit. These sub-sections are helpful when navigating the standard and provide clarity over which requirements apply in a given engagement's circumstances.

These sub-sections also aid the scalability of the standard and may be particularly helpful to smaller group audit engagements performed entirely by the group engagement team (for example, if the group entities are all audited by the same team from a single office).

See our response to question 11 for specific suggestions related to the presentation of requirements related to referred-to auditors.

3. Is the scope and applicability of the proposed SAS clear? In that regard, is the definition of group financial statements, including the linkage to a consolidation process, clear?



We generally believe the scope and applicability is clear. We also support the intent of the change in definition of group financial statements and the linkage to a consolidation process. We appreciate that the proposed SAS gives further guidance on how to consider shared service centers when planning and performing a group audit, as these structures are becoming ever more integral to record-keeping and financial reporting, and as a result, are of increasing importance to an auditor's understanding of the group's system of internal control. As noted in our response to question 1, we believe further guidance on sharing evidence obtained from testing at a shared service center could be useful.

See also our response to question 4.

4. With respect to the scalability of the proposed SAS

- a. do you believe the proposed SAS is scalable to groups of different sizes and complexities, recognizing that group financial statements, as defined in the proposed SAS, include the financial information of more than one entity or business unit? If not, what suggestions do you have for improving the scalability of the proposed SAS?
- b. do you believe that the guidance in exhibit A, "Relevancy of Requirements in Various Group Audit Scenarios," of the proposed SAS is understandable and provides clarity on the relevancy of certain requirements of the proposed SAS in various group audit scenarios? Would the relevancy of certain requirements of the proposed SAS in various group audit scenarios be clear without exhibit A?

Scalability

While we generally believe the proposed SAS is scalable to groups of different sizes and complexities, further guidance is necessary in a number of areas to promote more consistent application of the principles-based requirements in the proposed SAS.

It is important that the proposed SAS supports auditors in being able to scope and plan the audit based on the nature and circumstances of the group, and recognizes the important roles both group and component auditors play in contributing to group audit quality. In this regard, it is important that, in moving away from some well-recognized concepts in extant AU-C section 600 (e.g., significant components), the ASB is satisfied that the proposed SAS continues to support high-quality group audits, including consistent judgments about scoping of the group audit and the nature, timing, and extent of the involvement of component auditors.

For example, extant AU-C section 600 established specific requirements when a significant component is identified by the group engagement team, which is defined as a component that (i) is of individual financial significance to the group, or (ii) due to its specific nature or circumstances, is likely to include significant risks of material misstatement of the group financial statements. While we appreciate that the proposed SAS is aimed at promoting a risk-based approach rather than a quantitative exercise, we are concerned that the important principles underpinning these extant requirements are not given sufficient prominence, which could impact quality. We suggest changes to the application material to reinforce auditor judgments made in applying the requirements in paragraphs 24 and 39 of the proposed SAS. We believe certain concepts contained in the PCAOB's standards could be incorporated to drive further consistency in the US in terms of these judgments about how best to address risks of material misstatement in the group financial statements. We also believe further examples as to when specific further audit procedures may be used would be helpful. See paragraphs A59 and A145 in Appendix 2

Review of component auditor work

Also with regard to question 4a, we note the new requirement in paragraph 49 for the group auditor to determine whether, and the extent to which, it is necessary to review additional component auditor documentation. We believe it is important that the group auditor be able to exercise professional



judgment in relation to the nature, timing, and extent of review of the work of component auditors, taking into account the two-way communication that has occurred throughout the audit. In many cases, the group auditor may not consider it necessary to obtain and review audit documentation beyond what is required to be provided by, and discussed with, the component auditor in accordance with paragraphs 47-48 of the proposed SAS.

Exhibit A

Exhibit A is understandable and provides clarity to help auditors navigate the standard for circumstances applicable to their audits. This may need to be supplemented with additional guidance to support the auditor's consideration of the nature, timing, and extent of direction, supervision, and review that may be necessary in relation to different types of group audits, including circumstances in which the group auditor and component auditor are not from the same network.

5. Do you support the enhanced requirements and application material on documentation, including the linkage to the requirements of AU-C section 230? In particular
- a. are there specific matters that you believe should be documented other than those described in paragraph 76 of the proposed SAS?
 - b. do you agree with the application material in paragraphs A203–A219 of the proposed SAS relating to the group auditor's audit documentation?

We do not have concerns about the enhanced requirements and application material on documentation. We did not identify any additional matters that we believe should be documented.

6. Are the definitions of the terms referred-to auditor, component auditor, and group auditor clear, including as they relate to the definition of the term engagement team in the proposed QM SAS?

Generally, we believe the definitions of the terms referred-to auditor, component auditor, and group auditor are clear. However, as described in our response to question 1, we believe that uncertainty remains as to the practical implications of the change in SAS 146 to include component auditors within the definition of engagement team. One example of this is the effect on compliance with independence and ethical requirements.

7. Is the requirement in paragraph 11 [of AU-C section 300] clear? Are there additional requirements or application material relating to paragraph 11 that are needed, and if so, what should they be?

Yes, the proposed changes to the requirement in paragraph 11 of AU-C section 300 related to the engagement partner's review of the overall strategy and audit plan is clear. We note the effect of this change (which was approved by the ASB in finalizing SAS 146) is to extend the requirement in paragraph 19 of extant AU-C section 600 in relation to the group audit strategy and group audit plan to all audits (not just group audits). We do not believe additional requirements or application material related to paragraph 11 are necessary. However, the ASB should consider whether additional guidance is needed if questions arise during exposure in relation to how this requirement would be implemented for all audits (e.g., in relation to how detailed the overall strategy and audit plan needs to be and how technology may be used to facilitate the development and review of the overall strategy and plan).

8. Do you agree with the deletion of this requirement [paragraph 14(b) of AU-C section] and the related application paragraph? Do you have other suggestions for considering components in interim reviews now that the concept of "significant components" has been eliminated?



Yes, we support deletion of the requirement and related application material in AU-C section 930, which required the auditor to obtain reports from component auditors, if any, related to reviews performed of the interim financial information of significant components of the reporting entity. In practice, we believe auditors would look to the proposed SAS and make appropriate requests for component auditors to be involved in an interim review if necessary to do so.

9. Do you agree with the application material in paragraphs A47–A49 of the proposed SAS relating to a noncontrolling interest in an entity that is accounted for by the equity method? Are there additional requirements or application material relating to EMIs that are needed in the proposed SAS, and if so, what should they be?

We believe the application material in paragraph A10 of the proposed SAS relating to circumstances in which the auditor intends to use work already performed on component financial statements for purposes of the group audit is helpful, as is the specific application material in paragraphs A47-A49 relating to a noncontrolling interest in an entity that is accounted for by the equity method when access is restricted.

We believe, however, that there may be merit in being more clear that the guidance in paragraphs A47-A49 may be more widely applicable and suggesting an alternative approach to obtaining audit evidence in relation to equity method investees.

In its Other Auditor project, we note that the PCAOB has decided to no longer require the investor's auditor to supervise the investee's auditor's work in accordance with AS 1201. Appendix B of AS 1105, which was finalized in connection with the PCAOB's Estimates project, provides helpful context in evaluating the relevance and reliability of audit evidence associated with the valuation of investments based on investee financial results. Other proposed amendments to AS 1105 clarify that the group auditor's (lead auditor's in PCAOB terminology) assessment of audit evidence associated with audited financial statements of equity method investees is not intended to classify the investee's auditor as an component auditor (other auditor in PCAOB terminology).

10. Do you support retaining the option that exists in extant AU-C section 600 for the group engagement partner to make reference to the audit of a referred-to auditor (a component auditor per extant AU-C section 600) in the auditor's report on the group financial statements?

Yes, we support retaining the option to make reference to the audit of a referred-to-auditor.

11. Are the specific requirements relating to referred-to auditors clear, appropriate, and easily identifiable within the proposed SAS, including when considering exhibit A?

The requirements in the proposed SAS are intended to both leverage extant requirements and mirror the structure of the responsibilities of the group auditor in relation to component auditors. In our view, the requirements in the proposed SAS appear to be more restrictive than the requirements proposed by the PCAOB when dealing with referred-to auditors. For example, proposed PCAOB AS 1206 does not have a requirement to communicate significant risks to referred-to auditors, while the proposed SAS requires that the group auditor communicate significant risks that are relevant to the referred-to auditor. There may be practical challenges with this and other requirements (e.g., determining that referred-to auditors have the appropriate competence and capabilities) based on the level of access and communication the group engagement team is able to have with a referred-to auditor. Our view of the PCAOB's proposed standard is that, while there are inquiries of, and representations from, the referred-to auditor, the expectation of the two-way dialogue between the group auditor and the referred-to auditor is substantially less than what would be anticipated between the group auditor and the component auditor.



We question if the effort required by the proposed SAS is necessary for non-public companies audited under ASB standards as compared to public companies audited under PCAOB standards. Because the concept of referred-to auditors is unique to the US environment, we encourage the ASB to seek closer alignment with the PCAOB in setting its requirements, given the PCAOB's plans to finalize its standard in the near future.

Additionally, the construct of the standard has resulted in a level of repetition that might render it unclear. Clarifications to the wording and ordering of certain requirements would better follow the flow of the audit process and assist the auditor's judgment in first deciding whether it is appropriate to make reference, and then how to do so. We also believe the ASB could seek to reduce the degree of duplication between a number of requirements, specifically in relation to independence and relevant ethical requirements. We offer some drafting suggestions in Appendix 2, but believe there may be further opportunities to streamline.

Finally, we appreciate the focus in the requirements on the implications when the referred-to auditor has performed the audit in accordance with auditing standards other than GAAS or those of the PCAOB, as well as when the component's financial statements are prepared using a different financial reporting period from that used for the group financial statements. However, in terms of additional guidance, the ASB could consider elaborating on the audit implications when referring to another auditor in circumstances where the component financial statements are for a different financial reporting period than that of the group (as contemplated by paragraphs 42 and A113 of the proposed SAS).

12. Is the last sentence of paragraph A41 clear? Is there additional application material that is needed, and if so, what should it be?

We agree the last sentence of paragraph A41 is clear.

13. Does the proposed effective date provide sufficient time for preparers, auditors, and others to adopt the new standard and related conforming amendments, including sufficient time to support effective implementation of the proposed SAS?

We appreciate that the ASB has aligned the proposed effective date of the proposed SAS with the effective date of SAS 146. We believe the proposed effective date provides sufficient time for effective implementation.



Appendix 2 - Drafting suggestions

This Appendix provides our detailed drafting suggestions based on our comments provided in Appendix 1 and other editorial comments. Suggested additions are indicated in underlined text. Suggested removals are indicated in ~~strikethrough text~~.

Introduction

Scope of this Proposed SAS

...

Involvement of Component Auditors

.8. The group auditor may involve component auditors to provide information, or to perform audit work, to fulfill the requirements of this proposed SAS. Component auditors may have greater experience with, and a more in-depth knowledge of, the components and their environments (including local laws and regulations, business practices, language, and culture) than the group auditor. Accordingly, component auditors can be, ~~and often are,~~ involved in all phases of the group audit under the direction and supervision of the group auditor. (Ref: par. A10–A11) ~~[To further differentiate component auditors and referred-to auditors and to temper discussion of the use of component auditors]~~

...

Making Reference to the Audit of a Referred-To Auditor

.10 In accordance with t~~This proposed SAS, ~~also describes the procedures to be followed to obtain sufficient appropriate audit evidence when the group engagement partner can also~~ determines to make reference to the audit of a referred-to auditor in the auditor's report on the group financial statements in circumstances when the referred-to auditor has performed an audit of the financial information of a component. Reference in the auditor's report on the group financial statements to the fact that part of the audit was conducted by a referred-to auditor communicates the source of audit evidence with respect to those components for which such reference is made. Because the group auditor does not direct, supervise, or review the work of a referred-to auditor, a ~~A~~-referred-to auditor is not a component auditor, and accordingly, a referred-to auditor is not a part of the engagement team. Therefore, when the terms *component auditor* and *engagement team* are used in this proposed SAS, they do not include referred-to auditors. The requirements in paragraphs .51-.65 and the related application material are specific to referred-to auditors. Paragraphs .51-.57 set out requirements to enable ~~Therefore, when the group engagement partner to determine whether plans to make reference to the audit of a referred-to auditor in the auditor's report on the group financial statements when establishing the overall group audit strategy and group audit plan in accordance with paragraph 24 of this proposed SAS. The these requirements in paragraphs .58-.65, in addition to other requirements related to the execution of the group audit, are relevant when the group engagement partner determines to make reference. [To further tee up the concept of referred-to auditors and separate the requirement to determine if it is appropriate to make reference]]~~~~

...

Responsibilities of the Group Engagement Partner and Group Auditor

13. The group engagement partner remains ultimately responsible, and therefore accountable, for compliance with the requirements of this proposed SAS. Nevertheless, the group engagement partner may seek assistance from others to fulfill these responsibilities. The phrase “the group engagement partner should take responsibility for...” or “the group auditor should take responsibility for...” is used for those requirements for which ~~when~~ the group engagement partner or group auditor, respectively, is permitted to



assign the design or performance of procedures, tasks, or actions to ~~the~~ appropriately skilled or suitably experienced members of the engagement team, including component auditors. For other requirements, this proposed SAS expressly intends that the requirement or responsibility be fulfilled by the group engagement partner or group auditor, as applicable, and in such circumstances, the group engagement partner or group auditor may need to obtain information from the firm or other members of the engagement team. For example, when others, including component auditors, perform supervisory and review activities, the outcome of those activities can be taken into account by the group engagement partner in fulfilling these responsibilities. (Ref: par. A19, A33) [To align with paragraph 9 of SAS 146]

...

Definitions

16.

component auditor. An auditor who performs audit work related to a component for purposes of the group audit under the direction and supervision of the group auditor. A component auditor is a part of the engagement team⁴ for a group audit. A referred-to auditor is not a component auditor, and accordingly, is not a part of the engagement team for a group audit. (Ref: par. A23–A26) [To reiterate the difference between component auditors and referred-to auditors]

Requirements

...

Overall Group Audit Strategy and Group Audit Plan

.24 In applying AU-C section 300,⁵ the group auditor should establish, and update as necessary, an overall group audit strategy and group audit plan. In doing so, the group auditor should determine the following: (Ref: par. A54–A58)

...

- c. The components for which, if any, the auditor's report on the group financial statements will make reference to the audit of a referred-to auditor when the group auditor has determined it is appropriate to do so in accordance with the requirements of paragraphs .51-.5765). [To note that this is a specific judgment that must be made]

...

Considerations When Component Auditors Are Involved

.33 The group auditor should communicate the following to component auditors on a timely basis: (Ref: par. A116)

- a. Matters that the group auditor determines to be relevant to the component auditor's design or performance of risk assessment procedures for purposes of the group audit, including identified significant risks of the group financial statements that are relevant to the work of the component auditor [To be consistent with the other bullets and reiterate that the communications focus on what is relevant to the work being performed at the component vs. suggesting all significant risks of the group financial statements are relevant to the component]

...

⁴ Paragraph 12 of QM SAS

⁵ Paragraphs 7-10 of AU-C section 300



Considerations Regarding Making Reference to the Audit of a Referred-to Auditor in the Auditor's Report on the Group Financial Statements

Understanding the Referred-To Auditor and Determining Whether to Make Reference

Relevant Ethical Requirements, Including Those Related to Independence, for Referred-To Auditors

.51 When making reference to the audit of a referred-to auditor, the group engagement partner should take responsibility for (Ref: par. A165)

- a. obtaining an understanding of whether referred-to auditors have ~~being~~ been made aware of relevant ethical requirements that are applicable given the nature and circumstances of the group audit engagement; and ~~[To align more closely with extant AU-C section 600. Note that the PCAOB standard simply requires a written representation that the referred-to auditor is independent similar to paragraph 63; also note this is somewhat duplicative of paragraph 62]~~

...

Competence and Capabilities of Referred-To Auditors

.52 When making reference to the audit of a referred-to auditor, the group engagement partner should take responsibility for understanding whether ~~determining that~~ referred-to auditors have the appropriate competence and capabilities. (Ref: par. A166–A168) ~~[To align more closely with extant AU-C section 500. Note that the PCAOB standard requires the lead auditor to make inquiries of the referred-to auditor and look to other information obtained during the audit]~~

~~.53 The group auditor should obtain sufficient appropriate audit evidence relating to the work to be performed at the component without making reference to the audit of a referred to auditor in the auditor's report on the group financial statements if: (Ref: par. A169–A170)~~

- ~~a. the referred to auditor does not comply with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement; or~~
- ~~b. the group engagement partner has serious concerns about the matters in paragraphs .51-.52. [Moved below to assist in the flow of the requirements]~~

Consolidation Process Considerations for Referred-To Auditors

~~.534~~ When making reference to the audit of a referred-to auditor, the group auditor should obtain an understanding of whether the group auditor will be able to obtain information affecting the consolidation process from group management or a referred-to auditor.

Determining Whether to Make Reference to the Audit of a Referred-To Auditor (Ref: par. A171–A178)

~~.545~~ Having obtained an understanding of the referred-to auditor in paragraphs ~~.51–.53~~~~54~~, the group engagement partner should determine whether to make reference to the audit of a referred-to auditor in the auditor's report on the group financial statements.

~~.556~~ Reference to the audit of a referred-to auditor in the auditor's report on the group financial statements should not be made unless:

- a. ~~the group engagement partner has determined that the~~ referred-to auditor has performed an audit of the financial statements of the component in accordance with the relevant requirements of GAAS or the standards promulgated by the PCAOB (Ref: par. A174), and



b. the referred-to auditor has issued an auditor's report that is not restricted as to use.

.56 The group auditor should obtain sufficient appropriate audit evidence relating to the work to be performed at the component without making reference to the audit of a referred-to auditor in the auditor's report on the group financial statements if: (Ref: par. A169–A170)

a. the referred-to auditor does not comply with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement; or

b. the group engagement partner has serious concerns about the matters in paragraphs .51.52. [Moved from above, this is not explicitly addressed in PCAOB standards]

...

Subsequent Events

.66 In applying AU-C section 560,⁶ the group auditor should take responsibility for performing procedures, including, as appropriate, requesting component auditors or referred-to auditors to perform procedures, designed to identify events that may require adjustment of, or disclosure in, the group financial statements. (Ref: par. A185–A187)

Considerations When Component Auditors or Referred-to Auditors Are Involved

.67 The group auditor should request the component auditors and referred-to auditors, as applicable, to notify the group auditor if they become aware of subsequent events that may require adjustment of, or disclosure in, the group financial statements. (Ref: par. A187) [This requirement is equally relevant to referred-to auditors, could consider placing it elsewhere]

...

Evaluating the Sufficiency and Appropriateness of Audit Evidence Obtained

...

.69 The group engagement partner should evaluate the effect on the group audit opinion of any uncorrected misstatements (whether identified by the group auditor or communicated by component auditors) or other communications from component auditors and, as applicable, referred to auditors, including and any instances when there has been an inability to obtain sufficient appropriate audit evidence. (Ref: par. A193) [To encourage auditors to consider any additional information from referred-to auditors]

* * *

Application and Other Explanatory Material

Components at Which to Perform Audit Work (Ref: par. 24a)

A59. The determination of components at which to perform audit work is a matter of professional judgment. The following are examples of matters that may influence the group auditor's determination:

- The nature and significance of individual entities or business units included in the group financial statements, including the nature of events or conditions that may give rise to risks of material misstatement at the assertion level of the group financial statements that are associated with a component, for example
 - newly formed or acquired entities or business units,
 - entities or business units in which significant changes have taken place,

⁶ Paragraphs 9-10 of AU-C section 560, Subsequent Events and Subsequently Discovered Facts



- significant transactions with related parties,
 - significant unusual transactions, and
 - abnormal fluctuations identified by analytical procedures performed at the group level, in accordance with AU-C section 315.
- The specific risks associated with an individual entity or business unit, including whether those risks
 - represent significant risks or
 - apply to other entities or business units included in the group financial statements, such that these risks, in combination, represent a risk of material misstatement
 - The disaggregation of significant classes of transactions, account balances, and disclosures in the group financial statements across components, considering the size and nature of assets, liabilities, and transactions at the location or business unit relative to the group financial statements
 - Whether sufficient appropriate audit evidence is expected to be obtained for all significant classes of transactions, account balances, and disclosures in the group financial statements from audit work planned on the financial information of identified components
 - The nature and extent of misstatements or control deficiencies identified at a component in prior period audits
 - The nature and extent of the commonality of controls across the group and whether, and if so, how, the group centralizes activities relevant to financial reporting [To incorporate additional guidance related to the extant concepts of significant components and the type of work to be performed as well as guidance from PCAOB AS 2101]

...

Resources (Ref: par. 24b)

...

A62. Component auditors may be involved in different phases of an audit. For example, component auditors may design or perform

- risk assessment procedures, ~~and/or~~
- procedures to respond to the assessed risks of material misstatement.

...

The Nature and Extent of Further Audit Procedures

A144. In applying AU-C section 330, the nature, timing, and extent of further audit procedures at components are expected to be based on, and responsive to, the assessed risks of material misstatement of the group financial statements. In response to the assessed risks of material misstatement, the group auditor may determine the following scope of work to be appropriate at a component (with the involvement of component auditors, as applicable):

- Design and perform further audit procedures on the entire financial information of the component
- Design and perform further audit procedures on one or more classes of transactions, account balances, or disclosures



- Perform specific further audit procedures

...

Design and Perform Further Audit Procedures on One or More Classes of Transactions, Account Balances, or Disclosures

A148. The group auditor may determine that designing and performing further audit procedures on one or more particular classes of transactions, account balances, or disclosures of the financial information of a component is an appropriate approach to address assessed risks of material misstatement of the group financial statements. For example, a component may have limited operations but hold a significant portion of the land and buildings of the group or have significant tax balances. In such cases, the component auditor may exercise professional judgment in determining the nature, timing and extent of procedures to be performed, taking into account component materiality.

Perform Specific Further Audit Procedures

A149. The group auditor may determine that designing and performing specific further audit procedures on the financial information of a component is an appropriate approach, including to complement testing performed by the group auditor, such as when audit evidence needs to be obtained for one or more relevant assertions only. For example, the group auditor may

- centrally test the class of transaction, account balance, or disclosure and may require the component auditor to perform specific further audit procedures at the component (for example, specific further audit procedures related to the valuation of claims or litigations in the component's jurisdiction or the existence of an asset or the observation of inventory counts).
- request one or more component auditors to perform tests of controls related to significant classes of transactions, account balances, and disclosures.
- request a component auditor to perform procedures to obtain audit evidence related to one or more relevant assertions, and may specify the sample sizes to be used (e.g., in the case of a component auditor who is from a different network and therefore not subject to common audit methodologies or to drive consistency in testing across components with similar characteristics).