

## Group Audits: Discussion Memorandum and Issues

### Discussion of Comment Letter Responses to “Requests for Comment” in the Exposure Draft of Proposed SAS *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Auditors)*

#### I. Objectives of Agenda Item 2

- To obtain views from the Auditing Standards Board (ASB) on a draft of the March 23, 2022, exposure draft entitled Proposed Statement on Auditing Standards (SAS) *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Auditors)* (ED) that has been revised to respond to comments in comment letters and from members of the ASB at the July 19-21, 2022, ASB meeting.
- To provide the ASB with further feedback from comment letters on the ED.
- To obtain direction from the ASB about changes that should be made to the October 2022 draft of the ED to enable the ASB at its January 2023 meeting to discuss a revised draft and vote on whether the proposed SAS should be issued as a final SAS.

#### II. Group Audits Task Force

The following are the members of the Group Audits Task Force:

- Dora Burzenski, Chair; assisted by Lauren Kolarik
- Michael Bingham
- Monique Booker
- Harry Cohen
- Heather Funsch
- Clay Huffman
- Maria Manasses
- Staffed by Judith Sherinsky

#### III. Background

The proposed SAS addresses audits of group financial statements and, if issued as a final SAS, would supersede extant AU-C section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*. It is intended to strengthen the auditor's approach to planning and performing a group audit and to clarify the interaction of the proposed SAS with the other AU-C sections, including AU-C section 220, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*, AU-C section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, and AU-C section 330, *Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence*. In developing and updating its standards, one of the strategic objectives of the ASB is to converge its standards with those of the International Auditing and Assurance Standards Board (IAASB), while taking into consideration the standards of other standard setters, such as the Public Company Accounting Oversight Board (PCAOB) and the U.S. Government Accountability Office (GAO). The proposed SAS is based on International Standard on Auditing (ISA) 600 (Revised), *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*, which was approved at the December 2021 IAASB meeting and issued in April 2022.

At its July 19-21, 2022, meeting, the ASB discussed and provided preliminary recommendations regarding responses from commenters on the following four issues addressed by questions posed in the ED:

Issue 1: Auditing components that are equity method investments (EMIs) and consideration of alignment with PCAOB standards.

Issue 2: Structure of proposed standard related to referred-to auditors and consideration of alignment with PCAOB standards.

Issue 3: Considering the magnitude of the portion of the financial statements audited by referred-to auditors in determining whether sufficient appropriate audit evidence can reasonably be expected to be obtained (par. A41 of the ED).

Issue 4: Recommendation for PEEC to align with the IESBA project and to clarify independence requirements for group audits.

[Highlights](#) of the ASB's July 2022 discussion of group audits are included in this discussion memorandum.

#### IV. Agenda Materials

Agenda Item 2	Group Audits: Discussion Memorandum and Issues
Agenda Item 2A	October 2022 Draft of Proposed Statement on Auditing Standards <i>Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Auditors)</i> Marked from the March 23, 2022, Exposure Draft (including Conforming Amendments)
Agenda Item 2B	Summary of Comments on Exposure Draft Proposed SAS <i>Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-To Auditors)</i> and Responses to Comments
Agenda Item 2C	PCAOB AS 1206, <i>Dividing Responsibility for the Audit with Another Accounting Firm</i> , per PCAOB Adopting Release No. 2022-002 dated June 21, 2022
Agenda Item 2D	Appendix B, <i>Audit Evidence Regarding Valuation of Investments Based on Investee Financial Results</i> , of PCAOB AS 1105, <i>Audit Evidence</i> , per PCAOB Adopting Release No. 2022-002 dated June 21, 2022
Agenda Item 2E	AU-C 501, <i>Audit Evidence — Specific Considerations for Selected Items</i>

Ms. Burzenski will use agenda items 2 and 2A for discussion purposes..

## High Level Summary of Comment Letter Feedback

The ASB received 22 comment letters on the exposure draft (ED) of the proposed SAS, which seeks specific feedback from respondents on 13 different topics identified in the ED under the headings “Request for Comment.”

Overall, the responses to the ED were supportive of moving forward with convergence with ISA 600 (Revised), subject to further revisions to the ED to address comments received. Of note is that a number of respondents believe that certain aspects of the proposed SAS should be aligned with [PCAOB Release No. 2022-002](#).

At the end of this discussion memorandum is an [appendix](#) that contains comments on the ED in which respondents request actions that go beyond the charge of the Group Audits Task Force (task force), for example, requests for further implementation guidance outside of the proposed SAS and recommendations for the ASB to engage with the AICPA Professional Ethics Executive Committee (PEEC) on related independence matters. The task force is identifying these items so that the ASB can determine the appropriate actions to be taken in response to these comments.

## Issues for ASB Consideration

The Group Audits Task Force (Task Force) is seeking direction from the ASB on issues pertaining to feedback received in response to the following four “requests for comment” in the ED:

[Request for Comment 3](#): Scope and Applicability of Proposed SAS; Definition of Group Financial Statements

[Request for Comment 9](#): Components That Are Equity Method Investments

[Request for Comment 11](#): Requirements Related to Referred-to-Auditors

[Request for Comment 12](#): Magnitude of Portion of Financial Statements Audited by Referred-To-Auditor

The four issues above are discussed in this memo. All of the detailed responses to the requests for comment in the ED are contained in Agenda Item 2B.

In addition to discussing the four items above, the Task Force will address any other questions or comments on item 2A and 2B.

## Request for Comment 1a-c: Linkage of Proposed SAS To Other AU-C Sections

**Question 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 (now AU-C section 220 of SAS No. 146)? 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?

<b>Question 1a:</b> Does the proposed SAS have appropriate linkages to other AU-C sections and to the proposed SQMSs?	No. of Responses
Yes	19
Yes with suggestions	2
No comment	1
No. of comment letters	22

Two of the commenters refer to suggestions for improving linkages to recently issued SAS No. 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*, which they described in their responses to [questions 1b](#) and [1c](#).

<b>Question 1b:</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?	No. of Responses
Yes	15
No comment	7
No. of comment letters	22

<b>Question 1b:</b> Are there other special considerations for a group audit that you believe have not been addressed in the proposed SAS?	No. of Responses
OK as is	8
Suggestions	3
No comment	11
No. of comment letters	22

Three commenters provided the following suggestions:

- SAS No. 146, *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*, (now AU-C section 220) and Statement on Quality Management Standards (SQMS) 1, *A Firm's System of Quality Management*, (now QM section 10) were issued in June 2022. Because the proposed group audits SAS was still under development at that date, changes to SAS No. 146 and SQMS 1 to conform with the proposed group audit SAS or to improve the interaction between these standards through supplemental guidance could not be made. The commenter recommends that the following conforming changes to SAS No. 146 and SQMS 1 be made:

SAS 146.31b	This paragraph requires additional guidance to assist auditors in understanding how to accomplish such a review in a group audit. It is not practical to assume that an auditor can
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	summarize all significant judgments for an engagement partner to review directly. Instead, it is more operational for the engagement partner to take responsibility for such reviews with the assistance from others. (GT)
SAS 146.34	This paragraph could be enhanced with application guidance specific to group audits as it may be difficult for the group engagement partner to be aware of all formal communications made by a component auditor to (1) management, (2) those charged with governance, or (3) regulatory authorities, some of which may also not pertain to the audit of the group financial statements. (GT)
SAS 146.41b	It is unclear how this requirement interacts with paragraph 76 of the group audits proposed SAS. Guidance that addresses this interaction and the expectations for the group engagement partner regarding component consultations would be beneficial. (GT)
SQMS 1.A14	To help bridge the gap between guidance provided in SAS 146 and the application of such guidance in the other sets of standards that would be subject to SQMS 1, add the following language:  Referred-to auditors are not members of the engagement team. Referred-to auditors are not component auditors. Likewise, in an examination or review engagement, when a firm determines to make reference to the examination or review of another auditor, accountant, or practitioner, the other auditor also is not a member of the engagement team. (GT)
SQMS 1.A91	To further clarify the various resources that may be used in an engagement subject to SQMS 1, add the following language:  Determining whether another auditor, accountant, or practitioner is a resource or an information source depends on the particular circumstances. For example, a component auditor is a resource used in performing a group audit, but a referred-to auditor is an information source, as a referred-to auditor's report provides information to be used as audit evidence. Similarly, a service auditor that issues a report on a service organization's controls is an information source and not a resource, unless the service organization is requested to perform further procedures for purposes of the particular engagement. A predecessor auditor, accountant, or practitioner is not a resource. (GT)

- Application guidance is needed to address how a group auditor gains comfort with a component auditor of a foreign company that conducts the audit in a foreign language, specifically
  - overcoming language barriers
  - related supervision requirements as well as guidance regarding a situation where a client wants to use a local firm that speaks a different language than the group auditor. (ICPAS)
- Paragraph 74b includes a requirement to communicate with those charged with governance of the group “instances where the group auditor’s review of the work of a component auditor gave rise to concern about the quality of that component auditor’s work, and how the group auditor addressed the concern.” The commenter believes this requirement is intended to be a follow up to the requirement in paragraph 74a related to communication of planned involvement in the work to be performed by component auditors. However, the commenter is concerned that the standard will lead to inconsistent application because
  - there will be various interpretations of what rises “to a concern about the quality of that component auditor’s work” given the lack of application material.

- there may be unconscious bias in that judgement when assessing component auditors from the group auditor's firm or network versus when the component auditor in an unrelated, competitor firm.

As a result, the commenter is concerned that the standard will not fully achieve its intentions related to communications with those charged with governance. (Mazars)

<b>Question 1c:</b> Does the proposed SAS result in a group audit that achieves the objectives of the proposed QM SAS?	<b>No. of Responses</b>
Yes	15
Suggestions	1
No comment	6
No. of comment letters	22

One commenter noted the importance of the requirements in the proposed SAS being clear insofar as how they interact with the requirements in SAS 146 and SQMS 1. The commenter believes that 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. The commenter encourages 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. The commenter also suggests that after the proposed SAS is implemented, the ASB seek feedback from the Peer Review Board and others to understand whether the proposed SAS and SAS 146 are achieving their intended objectives. The same commenter agrees 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, the commenter thinks it important that there be shared accountability for quality when firms use component auditors and encourages 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. (PwC)

### **Request for Comment 2: Structure of the Proposed SAS**

<b>Question 2:</b> With respect to the structure of the proposed SAS, do you support the placement of sub-sections 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?	<b>No. of Responses</b>
Yes	18
Suggestions	2
No comment	2
No. of comment letters	22

Two respondents commented on the formatting, recommending that the draft include icons, underlining, or other formatting to visually differentiate the component auditor subsections from the referred-to auditor subsections. One commenter noted that the subheadings one level below the headings are the same font size and type as the paragraphs themselves and that different formatting, such as underlining, should be used to enhance their visibility among the paragraphs. (GAO and GT)

### **Request for Comment 3: Scope and Applicability of Proposed SAS; Definition of Group Financial Statements**

<b>Question 3:</b> Is the scope and applicability of the proposed SAS clear? In that regard, is the definition of
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*group financial statements*, including the linkage to a consolidation process, clear?

Question 3: Is the scope and applicability of the proposed SAS clear?	No. of Responses
Scope and applicability are clear	15
Scope and applicability are unclear	4
No comment	3
No. of comment letters	22

The following are suggestions about how to improve the clarity of the scope of the proposed SAS and other comments from four commenters who believe the scope and applicability are not clear:

- The proposed SAS lacks clarity on what constitutes a “business unit” as that term is used in the definition of group financial statements. (VSCPA COV) (This comment also applies to the portion of question 3 about whether the definition of *group financial statements* is clear.)
- The proposed SAS should go beyond the reference to the Audit and Accounting Guide *State and Local Governments* and add a section on “Considerations Specific to Governmental Entities,” to address group audits of governmental component units, similar to other AU-C sections. (MI OAG) (Another commenter made the same suggestion in response to question 12.)
- There is still some ambiguity in regard to smaller, less complex entities that have different entities established for risk mitigation or through prior acquisitions. Some of these entities are structured to have a single or overall accounting department with the same system of internal control and, while certain portions of the operations are maintained separately, the financial information is not presented as disaggregated for external reporting purposes (particularly paragraph A127 in AU-C section 320 and the reference to what is defined as financial information that is disaggregated, as either internal only, or externally presented). (SL)

Question 3: In that regard, is the definition of <i>group financial statements</i> , including the linkage to a consolidation process, clear?	No. of Responses
Definition of GFS is clear	8
Definition of GFS is unclear	6
No comment	8
No. of comment letters	22

Six commenters believe the definition of group financial statements is unclear for the following reasons:

- The linkage between the definition of the “group financial statements” and “consolidation process” could be ambiguous under certain fact patterns that are common in practice. The application guidance in paragraphs A4 and A5 attempts to distinguish between two scenarios involving a single legal entity, where one involves the aggregation of financial information while the other doesn’t. Many legal entities are capable of maintaining discrete financial information associated with separate locations, branches, divisions, or product lines within a single general ledger system. For example, a retail entity may be capable of maintaining discrete financial information by individual store locations. The process of aggregating the financial information associated with retail store locations in this example is different from aggregating financial information prepared by one or more branches or divisions of a group that maintain separate information systems and general ledgers. The commenter recommends providing further clarity in the application material regarding the concept of “aggregation” of financial information of entities that is relevant to the

definition of group financial statements and the term *consolidation process* used in the proposed SAS to avoid any unintended consequences, including inconsistent application in practice. (BDO)

- The proposed SAS removes the link of group financial statements and components, which broadens the business units that could qualify for group financial statements. Specifically, paragraph A4 states “a single legal entity may be organized with more than one business unit ... when those business units have characteristics such as separate locations, separate management, **or** separate information systems.” The inclusion of “or” within the guidance is improper in a government environment as many business units have separate locations and separate management that are aggregated into a single legal entity’s financial statements; and, in many cases, we would not expect those to create a group audit scenario.

To align with the audit requirements for components throughout the proposed SAS, the commenter conceptually believes it is more logical to define a group as components aggregated through a consolidation process. To assist the auditor in identifying components (or business units) that trigger the group audit requirements, the commenter suggests that the Board further clarify the relevant criteria for assessing the extent to which separate locations, management, and information systems represent components (or business units) of a group. The following are questions the Board may consider in providing this guidance:

**Location:** Does the mere physical presence of the business unit within a separate building constitute a different location? Does the proximity of the business unit location to the group have any effect on the assessment (i.e., street address, campus, town, county, state, country)?

**Management:** In a government environment, authority may be delegated to various levels of management. For example, in producing an Annual Comprehensive Financial Report (ACFR), a Governor may delegate responsibility to an agency to produce the ACFR by aggregating financial information from other agencies. As it relates to aggregated Executive branch agencies, is the Governor and his or her administration considered management, or should consideration also be given to differences in agency-level management?

**Information Systems:** Does the significance of information systems to the financial statements (i.e., the general ledger) affect the assessment of the group? For example, if a business unit uses the same general ledger system as the group, but uses its own capital assets system, does the number of separate systems or materiality of financial amounts within the capital assets system affect the auditor’s assessment? (COV)

- With regard to paragraphs A29-A31 and the consolidation process, the commenter believes additional examples would be helpful and suggests that there be a more detailed example that expands the financial institution example introduced in paragraph A4. Paragraph A4 discusses operating in separate locations with multiple branches and how the separate characteristics, such as separate management or separate information systems (including a separate general ledger) are aggregated and how such financial statements meet the definition of group financial statements. The example could be a bank that has a holding company or other legal entity combined with the financial institution that is required to be consolidated. This may demonstrate the difference between aggregation risk considerations for an entity with multiple branches verses the aggregation risk considerations of consolidations.

Another common occurrence is when management, controls, processes, and information systems are the same for a group of consolidated entities. Consequently, some groups of consolidated entities may have less aggregation risk than others, which could significantly impact component materiality evaluations and audit approaches. Expanding A31 could provide needed practice



guidance in applying the standard to varying risk considerations. This would be particularly helpful as paragraph A7 appears to indicate that an engagement team could reach a conclusion that there's no aggregation risk in a consolidation when legally separate entities are under same management, controls, and information systems, etc.

For considerations specific to Government Entities, paragraph 3 of the ED references the AICPA Audit and Accounting Guide *State and Local Governments* which is a non-authoritative guide. It would be beneficial to expand the application and explanatory material with specific examples for government entities as opposed to referencing a non-authoritative guide. A common simple example that could be added is when a component unit is blended into a reporting unit. Another very common example is when the aggregate remaining reporting unit includes a number of unrelated activities under the same management, controls, process, and information systems and contrasting when there are disaggregated elements of the reporting unit. (Eide Bailly)

- The considerations in paragraphs A4 and A5 for determining whether the financial statements are group financial statements, include having separate locations, separate management, and separate information systems. Those same considerations could be used to conclude that a consolidated financial statement would not be a group financial statement; for example, if the separate legal entities have similar locations, management, and information systems. The definition of group financial statements in paragraph 16 appears to require that all consolidations be within the group audit scope, however there are situations in which closely held entities which legally may be consolidations, do not encompass the same risks and features that the group audit standards are intended to address. The commenter recommends that in addition to the examples in A4 and A5, a third example be provided to support and illustrate that the principles-based guidance can also be used to exclude a consolidated entity from being a group financial statement. (OSCPA NSAA)
- Provide more application guidance or other materials (e.g., a flowchart or decision tree) to help auditors with determining whether an engagement includes group financial statements, which is therefore subject to the scope of the proposed SAS. (CLA)

#### **Additional Information:**

##### Recap of IAASB History on Definitions

##### 1. Group Financial Statements

The IAASB discussed the definition of “group financial statements” several times throughout the drafting and exposure draft process because questions arose about the definition of that term. Throughout these discussions, the term “consolidation process” as an entry point for determining whether the financial statements are group financial statements was debated. The board discussed using the term “aggregation” rather than “consolidation” but ultimately decided that “consolidation” was a better term because it would be more understandable in the context of financial reporting frameworks. In response to the concern that “consolidation process” would be interpreted in the same way as the terms “consolidation” or “consolidated financial statements” as defined in other financial reporting frameworks, the IAASB task force added application paragraph A27 (paragraph A30 in the proposed SAS) to explain how “consolidation process” differs. Further, the IAASB explained that the specific terminology used is less important than the clarity of the fundamental principle in the revised standard and the focus on the process. They noted that although the process may differ somewhat depending on the nature and structure of the entity (i.e., the group), the process involves bringing together in a set of financial statements the financial information of more than one entity or business unit, with the elimination of intra-entity or business unit transactions or balances as needed. They also discussed that the term “consolidation process” is meant to capture not only consolidated financial statements, but more

broadly combined financial statements, equity-method investments, and the aggregation of the financial information of other entities or business units such as branches or divisions.

## 2. Business Unit / Component

During meetings on 3/16/20 and 12/7/20, the IAASB discussed the definitions of “component” and the term “business unit”. The meeting minutes indicate that the IAASB task force noted that the use of the terminology “entities or business units” in the definition of group financial statements may be viewed as somewhat broad and that entity management may use other terms to describe the various economic units. However, they noted that they believed that “entities or business units” will be sufficiently understood.

The IAASB discussed whether the definition of component should be from “management’s view” or the “auditor’s view” and ultimately concluded that it should be an audit-focused concept because the way management views the entities or business units comprising the group may be different from the way the group auditor plans and performs audit procedures for the group audit.

The board noted that the definition provides flexibility for the group auditor to determine components based on the group auditor’s understanding of the group and its environment. In the view of the IAASB task force, the definition highlights that the group auditor’s determination of components is based on the group’s organizational structure and information system, including its financial reporting process as required by ISA 315.

### **Task Force Response:**

As indicated in the summary of the IAASB minutes above, the definitions of “group financial statements” and “business units” were discussed at length and revised throughout the drafting process. The IAASB was careful to weigh the level of detail and examples provided in the ISA, while providing for flexibility in the principles-based framework.

In terms of the definition of “group financial statements,” although the task force understands that additional examples might provide auditors with a greater chance of having their engagement particulars line up directly with an example situation in the application guidance, the task force is reluctant to provide further examples to avoid changing the intent of the standard (e.g., through over-reliance on an example) and to ensure that the language remains broad enough and principles-based enough to provide a framework for all situations engagement teams may encounter.

Application paragraphs A4 and A5 in the proposed standard provide examples of scenarios in which the group financial statements are (paragraph A4) and are not (paragraph A5) group financial statements, which the task force believes is the appropriate balance in order to remain principles-based so that the standard can be applied across all types of engagements. Further, in considering whether a flowchart or decision tree should be added, the task force noted that past precedent indicates that such diagrams/graphics do not belong in the standard themselves and may instead, be provided as additional tools as deemed necessary outside the standards. The task force notes that providing such tools, similar to providing further examples, would go against the principles-based framework the ASB has set out to achieve with proposed AU-C 600.

Regarding the clarity of the term “business unit”, similar to the IAASB (as inferred from the summary of the minutes above), the task force is reluctant to provide additional examples that might limit the auditor’s flexibility to determine business units based on the group auditor’s understanding of the group and its environment (and the principles based requirements of the proposed SAS). Therefore, although the task force understands that there is ambiguity in exactly what constitutes a business unit, the task force believes it is appropriate to provide for application of the concept of business units across the large variety of entities audited under the AU-Cs.

For related comments applicable to governmental audits, the task force notes that the governmental audit guidance is outside of the charge of the task force and suggests that the ASB consider revisions to the

AICPA Audit and Accounting Guide *State and Local Governments* to ensure sufficient guidance is provided in light of this updated standard. (See the appendix containing comments that request actions that go beyond the charge of the task force). The task force believes there may be merit in considering additional guidance outside the standards post-implementation (e.g., Audit Risk Alert), when there is more information as to the nature of the difficulties auditors are encountering when applying the proposed SAS.

**Question for the ASB:**

1. Does the Board agree with the task force that additional application guidance or examples related to definitions in the proposed SAS are not necessary? If the Board disagrees, what additional application guidance or examples does the Board believe are necessary?

**Request for Comment 4: Scalability and Exhibit A, “Relevancy of Requirements in Various Group Audit Scenarios”**

**Question 4a-b:** 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?

<b>Question 4a:</b> Do you believe the proposed SAS is scalable to groups of different sizes and complexities, recognizing that <i>group financial statements</i> , 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?	No. of Responses
Yes	9
Yes with suggestions	7
No	4
No comment	2
No. of comment letters	22

Seven commenters had the following concerns and recommendations regarding the scalability of the proposed SAS:

- The proposed SAS presents additional practical challenges for the group engagement partner seeking to comply with the responsibilities in the proposed QM SAS with respect to determining compliance of component auditors with the relevant ethical requirements and the sufficiency and appropriateness of engagement resources, particularly on larger and more complex group audits that require extensive involvement of component auditors. These challenges are heightened in circumstances involving component auditors that are not part of the same network as the group auditor. (BDO)

- The commenter has practical concerns with regard to certain of the requirements specifically designated for execution by the group engagement partner, as described in paragraph 13 of the ED. For example, in AU-C section 300, the audit plan includes, among other things, the nature, timing, and extent of further audit procedures. In large group audits, it may be impractical for the group engagement partner to directly review, without assistance from others, all details of a group audit plan. Application material is necessary to address potential operational challenges, in group audits and to convey the intended purpose of the requirement and its practical application more clearly in group audits. (GT)
- With regard to 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, 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. (PwC)
- The proposed standard could be enhanced by providing additional application material with regard to how the auditor may use a completed audit of a component for purposes of the group audit. The commenter encourages the Board to add application material to paragraph 32a of the ED to explain that understanding the group may include understanding applicable statutory audit requirements of components and the timing of such audits. This information can help inform (1) the group auditor's consideration of where risks of material misstatement may arise within components and (2) the appropriate response to such risks. See also response to Question 9 below. (GT)
- The commenter submits the following edits to par. A144 to enhance the scalability and understandability of the guidance provided:
 

A144. 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 **(for example, when a component auditor is asked to perform an audit, adapted as necessary, of the component financial information for purposes of the group audit)**

Design and perform further audit procedures on one or more classes of transactions, account balances, or disclosures

Perform specific further audit procedures **designed by the group auditor** (GT)

The commenter also recommends adding an example similar to the first bullet above to proposed paragraph A120. (GT)
- In considering the existing requirements of AU-C section 300, the commenter believes that “key members of the engagement team” should be limited to the individuals that meet the definition of “group auditor” as defined in the proposed SAS. There could be unintended consequences of including component auditors as key engagement team members. As such, the commenter recommends revising paragraph A64 of the ED as shown below to clearly delineate what the group auditor is ultimately responsible for while also acknowledging that the component auditor can contribute to planning activities.
 

AU-C section 300 requires the engagement partner and other key members of the engagement team to be involved in planning the audit. When component auditors are involved, one or more individuals from a component auditor may ~~assist~~ **assist** ~~be key members of the engagement team and therefore involved~~ in planning the group audit.

The commenter indicates that such changes would also address the potential inconsistency in definitions and requirements between the proposed SAS and AU-C section 300. Paragraph .05 of AU-C section 300 requires the engagement partner and other key members of the engagement team to be involved in planning the audit, including planning and participating in the discussion among engagement team members. Planning an audit, as described in paragraph .02 of AU-C section 300, involves establishing the overall audit strategy and audit plan. The definition of group auditor, however, recognizes that the group auditor, which excludes component auditors, is responsible for establishing the overall group audit strategy and group audit plan. Including component auditors as key engagement team members can potentially blur a firm's responsibilities for the group audit opinion and also challenge whether the independence requirements would differ for such individuals, particularly when such individuals are outside the firm's network. (GT)

- When applying the risk-based approach prescribed in the proposed SAS, if the group audit firm differs from the component audit firm, use of different audit methodologies may present an issue. This is a challenge in terms of scalability of the standard, particularly in instances where there is a sub-consolidation performed by the component auditor. The commenter would like to see more guidance or tools on how the use of different audit methodologies by the component auditors is addressed by the group auditor, such as instances where testing approaches differ (i.e., sample sizes utilized for both tests of controls and tests of details). (ICPAS)
- The lack of guidance on how to determine the extent of work to be performed on components will lead to diversity in practice and the commenter recommends that the development of implementation guidance be considered related to scoping by component. (Mazars)
- The commenter refers to a concern related to the scalability to larger governments expressed in the commenter's response to question three. (NSAA)
- Extant AU-C section 600 establishes 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. The commenter appreciates that the proposed SAS is aimed at promoting a risk-based approach rather than a quantitative exercise but is concerned that the important principles underpinning these extant requirements are not given sufficient prominence, which could impact quality and suggests changes to the application material to reinforce auditor judgments made in applying the requirements in paragraphs 24 and 39 of the proposed SAS. 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. Also, further examples as to when specific further audit procedures may be used would be helpful. (See the edits to paragraphs A59 and A145 in Appendix 2 of the PwC comment letter.)

Four commenters believe the proposed SAS is not scalable to groups of different sizes and complexities for the following reasons:

- The scalability of the proposed SAS depends on clarifying the definition of a business unit, as mentioned in the commenter's response to Question 3. If separate locations, management, or information systems independently qualify as individual business units without application of professional judgement, implementation may be inefficient in a government environment. (COV) (VSCPA)
- Scalability is a more challenging concept to apply in group audits than in other standards. In other standards, scalability is an opportunity to adapt to less complex environments. In this standard,

the primary requirements are identifying the components, assessing aggregation risks, and developing responses to those risks. Accordingly, it's difficult to apply scalability considerations to these requirements. The most helpful guidance regarding potential scalability, (as noted in the commenter's responses regarding paragraphs A4, A7, and A31) is to develop application guidance that helps auditors determine when consolidations and certain other activities are not considered a group audit and/or do not have material aggregation risks. Additionally, upon determining that the audit is of a group financial statement, if there are opportunities to scale based on different sizes and complexities of group audits, the application guidance should provide more robust illustrations of such considerations. (Eide Bailly)

- The commenter requests examples of entities with less complexity where group audit procedures may be limited or reduced. (SL)

<b>Question 4b:</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?	<b>No. of Responses</b>
Clear and necessary	11
Clear (with suggestions) and necessary	2
Clear but unnecessary	1
Unclear but necessary	3
Unclear and unnecessary	1
No Comment	4
No. of comment letters	22

Four commenters found exhibit A to be unclear. The following are their suggestions to further clarify the exhibit and comments that identify what makes the exhibit unclear:

- Place exhibit A in the front of the draft instead of in the appendix ("start here"). (OSCPA)
- Provide additional guidance to help firms with the implementation of the proposed SAS for each of the scenarios in exhibit A. (CLA)
- For Scenarios 1 and 3, paragraph 36 is included as a relevant requirement and is under the heading "Considerations When Component Auditors Are Involved." Paragraph 36 is not intended to apply only when component auditors are involved and recommends deleting the heading and revising the paragraph as follows.

In applying AU-C section 315, the group auditor should evaluate whether the audit evidence obtained from the risk assessment procedures performed by the group auditor, and component auditors **when applicable**, provides an appropriate basis for the identification of assessment of the risks of material misstatement of the group financial statements. (GT NSAA)

- It is unclear why each scenario begins with paragraph 12 of the ED when the requirements section does not begin until paragraph 18. One commenter believes it is the Board's intention to only address the requirements section of the ED and, therefore, recommends revising each scenario to begin with paragraph 18. (GT) Another commenter recommends that the exhibit include references to paragraphs 1-11 as applicable for completeness, or further clarify why the relevant requirements included in exhibit A begin with paragraph 12 (when requirements in the proposed SAS start with paragraph 18). (KPMG)
- It might be helpful to simplify exhibit A to include scenarios that do not have multiple complex issues in a single example. (TXCPA)

- Despite the introductory paragraphs in exhibit A reminding group auditors that they are “required to have an understanding of the entire text of this proposed SAS, including its application and other explanatory material, to understand its objectives and apply its requirements properly”, we have concerns over implementation in practice. Specifically, the content in exhibit A may be misinterpreted as if only the requirements presented in tabular format in exhibit A are applicable in various group audit scenarios, which could lead to misapplication of the proposed SAS and a negative impact to audit quality. (KPMG)

#### Request for Comment 5: Documentation

**Question 5a-b:** Do you support the enhanced requirements and application material on documentation, including the linkage to the requirements of AU-C section 230? In particular

- are there specific matters that you believe should be documented other than those described in paragraph 76 of the proposed SAS?
- do you agree with the application material in paragraphs A203–A219 of the proposed SAS relating to the group auditor’s audit documentation?

<b>Question 5:</b> Do you support the enhanced requirements and application material on documentation, including the linkage to the requirements of AU-C section 230?	No. of Responses
Yes	17
No comment	5
No. of comment letters	22

<b>Question 5a:</b> Are there specific matters that you believe should be documented other than those described in paragraph 76 of the proposed SAS?	No. of Responses
OK as is	9
Additions	4
No comment	9
No. of comment letters	22

Nine commenters did not identify any specific matters that should be documented other than those in paragraph 76 of the proposed SAS. Four commenters had the following recommendations for specific matters that should also be documented:

- Consider requiring documentation of the requirements in 59c ii related to appropriateness of conversion entries. (CLA)
- Provide an explanation of how paragraph 76i. documentation of “The group auditor’s evaluation of, and response to, *findings or conclusions* of the component auditors or referred-to auditors about matters that could have a material effect on the group financial statements.” differs from pars. 76.g.ii. and 76.h.iii, which require documentation of matters related to communications with component auditors and referred-to auditors, respectively, “including how the group auditor has addressed *significant matters* discussed with” component auditors and referred-to auditors, respectively. (Crowe)
- If par. 76i is in part intended to allude to evaluating the referred to auditors’ issued report, and whether it includes any opinion modifications or other report modifications that may be relevant to the group auditor, clarify this by adding application guidance for paragraph 76i. (Crowe)

- Provide application material for situations in which the same firm conducts the audit of the component and is the group auditor. Paragraph A74 provides some guidance related to the determination of a component auditor's competency and capability. Paragraph A91 states that the form of communication would be affected when the group auditor and component auditor are from the same firm. Paragraph 76 states that the group auditor should include in the audit documentation all of the components noted in paragraph 76, such as competence and capability (par. 76c), the direction and supervision of the component auditors and review of their work (par. 76f). As noted in paragraphs A74, the firm's monitoring procedures and communication is relied on in these two examples. The firm has its own monitoring procedures to identify competency and has procedures for documenting evidence of review and has various levels of review. The extent of the documentation required by the group auditor in this example when the same firm conducts the audit of the component and is the group auditor would be an example where we suggest additional application guidance would be beneficial, specifically related to competency of the auditor, direction, supervision, and review of the component auditor's work within the same firm but different locations and teams. The application material should include whether it is expected that all of these elements are explicitly documented in the binder or is it sufficient to know that the firm's monitoring procedures cover the requirement related to competency, supervision, and review of the component auditor within the same firm (Eide Bailey)
- Provide additional discussion of documentation of risks and uncertainties that may be present at the component auditor level, including, but not limited to 1) local regulatory, 2) litigation, and 3) cyber related matters. (ICPAS)

<b>Question 5b:</b> Do you agree with the application material in paragraphs A203–A219 of the proposed SAS relating to the group auditor's audit documentation, including the linkage to the requirements of AU-C section 230?	<b>No. of Responses</b>
Yes	14
Yes, with suggestions	2
No	2
No comment	4
No. of comment letters	22

Two commenters did not agree with the application material in paragraphs A203-A219. The following are the suggestions for improving and the application guidance and comments from those who do not agree with the application guidance:

- When the retention of component auditor documentation is outside the control of the group auditor, it would be difficult for a firm to design and implement responses to address quality risks related to the quality objective in paragraph .32f of proposed SQMS No. 1. The ASB should consider enhancing the guidance in par. A206 to indicate that providing specific instructions to the component auditor would normally be a sufficient response to such quality risks. (CLA)
- Include a reference to the sufficiency of procedures performed by the component auditor in direct response to the identified group-level assessed risks of material misstatement. By removing the requirement to identify significant components, with more targeted risk-based procedures performed at the component audit level, there is added importance on ensuring sufficient procedures have been performed on overall risks of material misstatements assessed at the group level and relevant to the component auditor. (ICPAS)
- Paragraph A205 indicates that audit documentation comprises not only the documentation in the group auditor's file but also the separate documentation in the respective component auditor files



relating to the work performed by the component auditors for purposes of the group audit. Because of the potential ramifications from an audit quality as well as an inspection and regulatory perspective, particularly with respect to jurisdictions with confidentiality or professional secrecy restrictions, the commenter asks the ASB to consider adding guidance or requirements regarding what audit documentation would need to be retained in the group audit file to meet the objectives of AU-C section 230 and that would be sufficient from an external inspection perspective. (GT)

- Additional guidance would be beneficial regarding documentation of assessing component materiality. (OSCPA)

### **Request for Comment 6: Definitions of Terms *Referred-to Auditor, Component Auditor, Group Auditor and Engagement Team***

<b>Question 6:</b> Are the definitions of the terms <i>referred-to auditor, component auditor, and group auditor</i> clear, including as they relate to the definition of the term <i>engagement team</i> in the proposed SAS?	No. of Responses
All definitions are clear	14
All definitions are clear, with suggestions	1
Definition of component, component auditor, group auditor or referred-to-auditor is unclear	7
No. of comment letters	22

Eight commenters believe that 1 or more of the definitions are unclear. The following are the comments on the definitions and suggestion for improving them:

- *Component.* Because the commenter believes that the preparation of financial information is a key element of the identification of a component, the commenter recommends that the following language from extant AU-C 600 be reinstated in the definition of component “An entity or business activity for which group or component management prepares financial information that is required by the applicable financial reporting framework to be included in the group financial statements.” (Crowe)
- *Component.* The definition of component in paragraph 16 does not specifically mention that an equity method investee is considered to be a component. Although this is clarified in the definition of group financial statements, the Board should consider explicitly including equity method investees in the definition of component. (John Keyser)
- *Component auditor.* Paragraph A28 indicates that there may be joint engagement partners within a group auditor’s firm. Three commenters requested that the proposed SAS include a definition of *joint engagement partner*. They noted that in group audits where different components are audited by separate audit teams within the same firm under the direction of separate partners or partner equivalents they are unclear about whether these partners are “joint engagement partners” or “component auditors.” (COV, NSAA, MI OAG)
- *Component auditor.* In smaller firms in most cases, the group auditor performs both the role of the group auditor and component auditor at the same time. The commenter asks for another category or scalable considerations to the situation where the group auditor and component auditor are one and the same. (SL)
- *Component auditor.* 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. (PwC)

- *Component auditor.* Clarification is needed to distinguish the “group auditor” and “component auditor” within the context of the “engagement team” and to clearly delineate that the “referred-to auditor” is outside of the “engagement team.” (Application Material A19; A23). Perhaps a diagram or flowchart would be helpful in distinguishing these concepts. (ICPAS)
- *Component auditor.* Clarify the use of component auditors outside the group engagement team, or make the last sentence refer to involvement of component auditors outside the group engagement team. While the results of the engagement could be the same, additional documentation would be needed to clarify the use of component auditors, when the teams are the same, and would expand documentation to ensure all component auditor sections documentation is performed and recorded. (SL)
- *Group auditor.* Three commenters are concerned with the language of paragraph 16 and A85 which states, “the group auditor is responsible for directing and supervising the component auditors and review of their work.” Specifically, in the case of a group audit of a state’s ACFR performed by the same firm, does this guidance require that the engagement partner directly supervise all component auditors within the same firm? This is not efficient and is impractical given the engagement partner and component auditors will be operating under the same firmwide system of quality control. (COV, NSAA, MI OAG)

One of those commenters recommended broadening the definition of group auditor to read (insertions italicized): (NSAA)

*The firm comprised of the group engagement partner and members of the engagement team, including those component auditors who are within that same firm and follow the same system of quality control as the group engagement partner. The group auditor excludes all other than component auditors.*

If that change is made, the following edits would be needed for paragraph A23 (insertions italicized with strikeouts)

References in this proposed SAS to the engagement team, *as defined in QM SAS paragraph 12*, include the group auditor and component auditors. Component auditors may be from a network firm, a firm that is not a network firm, or the *same firm as the group engagement partner* ~~auditor’s firm (for example, another office within the group auditor’s firm).~~ *In the latter case, consideration as to whether the component auditors are part of the group auditor will depend on whether that component audit’s engagement team is under the same system of quality control as the group engagement partner.*

If these changes are considered, then the guidance in paragraphs 27 and 28 would need to be updated to include a reference to the group auditor, as appropriate.

## Request for Comment 7: Engagement Partner Should Review Overall Audit Strategy and Audit Plan

**Explanation:** The proposed SAS would add the following paragraph to AU-C section 300, *Planning an Audit*, and make it applicable to all audit engagements

11. The engagement partner should review the overall audit strategy and audit plan.

**Question 7:** Is the requirement in paragraph 11 clear? Are there additional requirements or application material relating to paragraph 11 that are needed, and if so, what should they be?

<b>Question 7:</b> Is the requirement in paragraph 11 clear?	No. of
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	Responses
Yes	19
No comment	2
No. of comment letters	21

<b>Question 7:</b> Are there additional requirements or application material relating to paragraph 11 that are needed, and if so, what should they be?	No. of Responses
Additions	2
OK as is	10
No comment	10
No. of comment letters	22

Two commenters who agreed that the requirements and application guidance are clear recommended the following changes:

Add “local business practices” to paragraph A17, first bullet. (CLA)

In AU-C section 300, the audit plan includes, among other things, the nature, timing, and extent of further audit procedures. In large group audits, it may be impractical for the group engagement partner to directly review, without assistance from others, all details of a group audit plan. Application material is necessary to address potential operational challenges, in group audits and to convey the intended purpose of the requirement and its practical application more clearly in group audits. (GT)

**Request for Comment 8: Deletion of Par. 14b in AU-C Section 930 Related To Reviews of Interim Financial Information Of An Entity That Prepares Group Financial Statements**

**Question 8:** Do you agree with the deletion of this requirement 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?

**Explanation:** The proposed SAS eliminates the concept of “significant components” and no longer includes a requirement for the group auditor to identify and audit significant components. Paragraph 14b of AU-C section 930, *Interim Financial Information*, includes a reference to significant components and requires the auditor, when conducting a review of interim financial information, to obtain reports from component auditors, if any, related to reviews performed of the interim financial information of significant components of the reporting entity, including its investees, or inquire of those auditors if reports have not been issued.

<b>Question 8:</b> Do you agree with the deletion of this requirement and the related application paragraph?	No. of Responses
Yes	17
No	3
No comment	2
No. of comment letters	22

Three commenters disagree with the deletion of this requirement and the related application paragraph for the following reasons:

- Related to the proposed edit to delete paragraph 14b and related application paragraph A17 of AU-C section 930, *Interim Financial Information*, we understand the need to modify 14b because

it includes the term “significant components”, which are no longer required to be identified in the proposed SAS. Par. A17 states “The auditor may find the guidance in section 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*, useful in conducting a review of interim financial information for an entity that prepares group financial statements.” The commenter finds this content to be relevant and meaningful even with the changes in the proposed SAS and recommends that par. A17 be retained in AU-C section 930 and included with another paragraph in the standard, if 14b is deleted. Alternatively, paragraph 14b could be modified, rather than deleted, to remove the reference to significant components and the requirement to obtain a report. (Crowe)

- We understand the Board’s basis for proposing to delete paragraph 14b of AU-C section 930; however, we note that the Board has retained an illustrative report example making reference to a referred-to auditor’s review report. The commenter is concerned that retaining the illustrative report example while deleting paragraph 14b and its related application material could lead to confusion. The commenter asks the Board to instead (1) revise 14b to require obtaining the referred-to auditor’s review report when the auditor plans to make reference to a referred-to auditor’s review report in the auditor’s review report on the group interim financial statements and (2) reinstate the application material that guides the auditor to consider AU-C section 600 in such circumstances. (GT)
- The commenter suggests modifying this paragraph instead of deleting the guidance altogether. Though the concept of significant components will be eliminated, we believe obtaining interim review reports on relevant elements of the reporting entity, if deemed appropriate by the group auditor to support their interim review procedures, remains an important procedure when performing the review of interim financial information under AU-C section 930. (ICPAS)

<b>Question 8:</b> Do you have other suggestions for considering components in interim reviews now that the concept of “significant components” has been eliminated?	<b>No. of Responses</b>
OK as is	7
Suggestions	3
No comment	12
No. of comment letters	22

Two commenters provided suggestions for considering components in interim reviews now that the concept of “significant components” has been eliminated and one commenter indicated that the reason for the elimination is not clear. The following are those comments:

- The commenter suggests that the ASB add a requirement under paragraph 14c for auditors conducting a review of interim financial information to make the following additional inquiry of management:  
***xiii. whether component auditors engaged to review interim financial statements of components, if any, communicated any material modifications that should be made to interim financial statements for them to be in accordance with the applicable financial reporting framework.***

The application paragraph in extant AU-C 600 would still be appropriate to support this requirement. (EY)

- The proposal should still provide the option to obtain such reports if based on the risk assessment, it is deemed necessary to do so for a particular component. (OSCPA)

- The commenter indicates that reason for the elimination is not clear. Consideration of materiality of a component should be considered when exercising a risk-based approach to the audit. (TXCPA)

### Request for Comment 9: Components That Are Equity Method Investments

**Question 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?

<b>Question 9:</b> 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?	No. of Responses
Yes	12
No	6
No comment	4
No. of comment letters	22

<b>Question 9:</b> Are there additional requirements or application material relating to EMIs that are needed in the proposed SAS, and if so, what should they be?	No. of Responses
Additions needed	9
OK as is	6
No comment	7
No. of comment letters	22

*(Note that the summary of responses have been reworded for brevity; see Agenda Item 2B for complete wording.)*

Four commenters (E&Y, GT, PwC, and KPMG) generally support aligning the proposed SAS with PCAOB standards on this topic. In particular, they note the potential audit evidence that can be obtained from audited financial statements as well as the challenges encountered by group auditors in establishing an arrangement with the auditor of an EMI under which the group auditor would direct and supervise the activities of the auditor of the EMI and review that auditor's work. These commenters generally recommended that the ASB align the proposed SAS with Appendix B, "Audit Evidence Regarding Valuation of Investments Based on Investee Financial Results," of PCAOB AS 1105, *Audit Evidence*, as amended in [PCAOB Release No. 2022-002](#) so that:

- If the audited financial statements of the EMI (including the accompanying auditor's report) are determined to constitute sufficient appropriate audit evidence, the auditor of the EMI would not be considered a component auditor (i.e., not part of the engagement team), and therefore, the group auditor would not be required to direct and supervise the auditor of the EMI or review that auditor's work.
- If the financial statements of the EMI are audited, the group auditor would be required to read the financial statements of the EMI and the accompanying auditor's report, perform limited procedures to determine whether the report is satisfactory for the group auditor's purpose, and if it is satisfactory, may be able to conclude that the financial statements and the auditor's report constitute sufficient appropriate audit evidence. These procedures are similar to those related to investments in securities

when valuations are based on the investee's financial results in extant AU-C section 501, *Audit Evidence – Specific Considerations for Selected Items*.

- If in the auditor's professional judgment additional audit evidence is needed, the group auditor would be required to perform procedures to gather such evidence.

Additionally:

- Three commenters requested that the ASB consider adding guidance that addresses situations in which no assurance exists relative to the EMI's financial statements (i.e., the EMIs did not obtain separate audits). (NSAA, MI OAG, COV) One commenter would like to see additional guidance, such as a materiality threshold, on whether a failure to obtain information would be considered a scope limitation, also noting that reverting to the cost basis is not appropriate. (TXCPA)
- One commenter indicates that a group auditor should only be following the guidance in paragraph A48 of the proposed SAS if the group financial statements include a noncontrolling interest in an entity that is accounted for by the equity method investment (which reflects a risk of material misstatement to the group financial statements) and the group auditor's access to information or people at the entity is restricted. The commenter is concerned that a group auditor may interpret the paragraph to mean that, even if they do not have specific access restrictions at the entity, they can directly apply A48 and obtain audited financial statements for the equity method investment and "take credit" for the substantive audit work performed on the equity method investment, without any interactions with the auditor of the equity method investment. To contribute to more consistent performance by group auditors, the commenter recommends that examples be provided to illustrate how differences in the risk assessment may impact the procedures performed by the group auditor. (Crowe)
- Two commenters believe paragraph A49 of the proposed SAS should be removed or updated because it suggests that restrictions on access to information or people of the equity method investee is an indicator that challenges management's assertion with regard to accounting for the investment under the equity method (management's assertion about the extent of influence it has on the EMI). Current accounting guidance regarding EMIs does not address restricted access in determining the extent of influence. The paragraph may be read to mean that the standard introduces additional considerations in determining the application of accounting standards. (CLA, Eide Bailly)
- In relation to EMIs, one commenter believes there should be consideration of a separate concept of component performance materiality. For example, an EMI that is 30% owned by the group should not have a component performance materiality of a comparative 100% owned component, as the risk of aggregated misstatements and risk of material misstatement represented by the 30% ownership is significantly less than another component of the same size. Expansion on determining component performance materiality for EMI would be helpful. (SL)

For ease of reference, the application material in paragraphs A47–A49 of the proposed SAS is as follows:

**A47.** In some circumstances, the group auditor may be able to overcome restrictions on access to information or people. Examples follow:

- If access to component management or those charged with governance of the component is restricted, the group auditor may request group management or those charged with governance of the group to assist with removing the restriction or otherwise request information directly from group management or those charged with governance of the group.

- If the group has a noncontrolling interest in an entity that is accounted for by the equity method, the group auditor may determine whether provisions exist (for example, in the terms of joint venture agreements or the terms of other investment agreements) regarding access by the group to the financial information of the entity and request group management to exercise such rights.
- If the group has a noncontrolling interest in an entity that is accounted for by the equity method and the group has representatives who are on the executive board or are members of those charged with governance of the noncontrolled entity, the group auditor may inquire whether they can provide financial and other information available to them in these roles.

**A48.** If the group has a noncontrolling interest in an entity that is accounted for by the equity method and the group auditor's access to information or people at the entity is restricted, the group auditor may be able to obtain information to be used as audit evidence regarding the entity's financial information, for example, from the following:

- Financial information that is available from group management because group management also needs to obtain the noncontrolled entity's financial information in order to prepare the group financial statements
- Publicly available information, such as audited financial statements, public disclosure documents, or quoted prices of equity instruments in the noncontrolled entity
- Financial statements audited by a referred-to auditor when the group auditor makes reference to the audit of a referred-to auditor in the auditor's report on the group financial statements

It is a matter of professional judgment, particularly in view of the assessed risks of material misstatement of the group financial statements and considering other sources of information that may corroborate or otherwise contribute to audit evidence obtained, whether the auditor can obtain sufficient appropriate audit evidence.

**A49.** If the group has a noncontrolling interest in an entity that is accounted for by the equity method and access to information or people at the entity is restricted, the group auditor may consider whether such restrictions are inconsistent with group management's assertions regarding the appropriateness of the use of the equity method of accounting.

The amended Appendix B, "Audit Evidence Regarding Valuation of Investments Based on Investee Financial Results," of PCAOB AS 1105, *Audit Evidence*, has been provided to the Board as Agenda Item 2E.

**Additional Information:**

Prior to extant AU-C 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)* becoming effective in 2012, the AU-Cs contained requirements that were similar to the PCAOB's (i.e., the ability to use audited financial statements as audit evidence for an investment accounted for using the equity method similar to investments in securities when valuations are based on the investee's financial results in extant AU-C section 501, *Audit Evidence — Specific Considerations for Selected Items* - see Agenda Item 2F). With the issuance of extant AU-C 600, it was clarified that equity method investments were considered "components", and paragraph AU-C 600.A23 elaborates on the ability to use audited financial statements as audit evidence, as follows:

A23. When access to information is restricted by circumstances, the group engagement team may still be able to obtain sufficient appropriate audit evidence; however, this is less likely as the significance of the component increases. For example, the group engagement team may not have access to those charged with governance, management, or the auditor (including relevant audit documentation sought by the group engagement team) of a component that is accounted for by the



equity method of accounting. If the component is not a significant component and the group engagement team has a complete set of financial statements of the component, including the auditor's report thereon, and has access to information kept by group management regarding that component, the group engagement team may conclude that this information constitutes sufficient appropriate audit evidence regarding that component. If the component is a significant component, however, and the auditor of the group financial statements is not making reference to the audit of a component auditor in the auditor's report on the group financial statements, then the group engagement team will not be able to comply with the requirements of this section that are relevant in the circumstances of the group audit. For example, the group engagement team will not be able to comply with the requirement in paragraphs .57–.58 to be involved in the work of a component auditor. Therefore, the group engagement team will not be able to obtain sufficient appropriate audit evidence regarding that component. The effect on the auditor's report of the group engagement team's inability to obtain sufficient appropriate audit evidence is considered in terms of section 705, Modifications to the Opinion in the Independent Auditor's Report.

### **Task Force Response:**

Comment letter responses to question 9 were preliminarily discussed with the ASB during the July 19-21, 2022, meeting as Issue 1, "Auditing Components That are Equity Method Investments (EMIs) and Consideration of Alignment with PCAOB Standards." [Highlights](#) of the July 2022 ASB discussion are included in this discussion memorandum.

Based on the comments received and direction from the ASB, the task force believes that the proposed SAS needs additional requirements and application material that address situations in which the group has a noncontrolling interest in an entity that is accounted for by the equity method and audited financial statements of the noncontrolled entity are available. The task force added the following material to the proposed SAS (see Agenda Item 2A):

### Requirements

- Item "d" in paragraph 24, which requires the group auditor, in establishing the group audit strategy, to determine whether to use the audited financial statements of an EMI as audit evidence regarding the EMI's financial results.
- Paragraph 65A, which contains required procedures the group auditor should perform when the group auditor intends to use audited financial statements of an EMI as audit evidence regarding the EMI's financial results. The requirements are similar to those in paragraph 5 of AU-C section 501<sup>1</sup> and paragraphs B1 and B5 of the amended Appendix B of PCAOB AS 1105.
- Item "h1" in paragraph 76, which requires the group auditor to document those components for which the group auditor uses audited financial statements of an EMI as audit evidence regarding the EMI's financial results.

### Application Material

- A sentence in paragraph A48, which indicates that regardless of whether the group auditor's access to information or people at the entity is restricted, if the group has an EMI and audited financial statements of the EMI are available, the group auditor may determine to use such audited financial statements as audit evidence regarding the EMI's financial results.
- Paragraph A65A, which outlines the following three approaches for auditing an EMI component :
  1. Treat the EMI auditor as a referred-to auditor and make reference to the audit of the EMI auditor in the auditor's report on the group financial statements,

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<sup>1</sup> Paragraph 5 of AU-C section 501 specifically excludes investments accounted for using the equity method of accounting.



2. Treat the EMI auditor as a component auditor and be involved in the EMI auditor's work
  3. Apply the newly added requirements (paragraphs 24d, 65A, and 76h.i) described above to use the audited financial statements as audit evidence (without making reference or being involved).
- Paragraph A173A, which addresses the difference between approaches 1 and 3 outlined in paragraph A65A.
  - Paragraphs A184A-A184D, which
    - identify matters for the group auditor to consider in determining whether the audited financial statements of an EMI and the accompanying audit report are satisfactory for use as audit evidence regarding the EMI. The matters are similar to those in paragraphs 13-14 of AU-C section 402, *Audit Considerations Relating to an Entity Using a Service Organization*; paragraph A10 of AU-C section 501; and paragraph B5 of the amended Appendix B of PCAOB AS 1105.
    - provide examples of situations in which additional audit procedures may be necessary to obtain sufficient appropriate audit evidence regarding the EMI. The examples are similar to those in paragraph A7 of AU-C section 501 and paragraph B2 in the amended Appendix B of PCAOB AS 1105.
    - provide examples of additional procedures the group auditor may perform in determining whether the audited financial statements of an EMI and the accompanying audit report are satisfactory. The examples are similar to those in paragraph A6 of AU-C section 501 and paragraph B1 (and the related footnote 1) in the amended Appendix B of PCAOB AS 1105.
    - provide guidance for situations in which the group auditor determines that the audited financial statements of the EMI and accompanying audit report are not satisfactory or do not provide sufficient appropriate audit evidence regarding the EMI's financial results.

**Question for the ASB:**

**2.** Do the proposed additions to the requirements and application material addressing situations in which the group has a noncontrolling interest in an entity that is accounted for by the equity method and audited financial statements of the noncontrolled entity are available, do the following :

- a. Address suggestions to align the proposed SAS with the amended Appendix B of PCAOB AS 1105 and AU-C section 501 on the topic of using audited financial statements of a noncontrolled entity?
- b. Provide sufficient guidance for group auditors to determine the audit approach for a noncontrolled entity? If not, what recommendations does the ASB have for further guidance?

**Request for Comment 10: Retaining the Option to Make Reference**

<b>Question 10:</b> 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?	No. of Responses
Yes	19
No comment	3
No. of comment letters	22

**Request for Comment 11: Requirements Related to Referred-to-Auditors**

<b>Question 11:</b> Are the specific requirements relating to referred-to auditors clear,	No. of
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appropriate, and easily identifiable within the proposed SAS, including when considering exhibit A?	Responses
Yes	13
Yes with suggestions	3
No	2
No comment	4
No. of comment letters	22

Three commenters had suggestions to improve the proposed SAS and two commenters believe that the requirements are not clear, appropriate, and easily identifiable for the following reasons:

- The commenter struggled to identify the requirements that would apply when component auditors and referred-to auditors are involved without reliance on the exhibit. To enhance the readability and ease of use, the commenter suggested that the ASB consider the following options:

*Issue a separate standard that includes the requirements and application material for circumstances when reference is made to the audit of a referred-to auditor in the auditor's report on the group financial statements:* The PCAOB took this approach in its proposal, since the referred-to auditor has a different level of supervision than a component team and is not part of the engagement team.

*Present the requirements for circumstances when reference is made to the audit of a referred-to auditor in the auditor's report on the group financial statements as a separate section within the SAS:* Though this would create some repetition in the proposed standard (i.e., requirements that apply to both the involvement of component auditors and referred-to auditors), it would enhance the clarity of the requirements and application when using a referred-to-auditor. (EY)

- The requirements in the proposed SAS appear to be more restrictive than the requirements in AS 1206, *Dividing Responsibility for the Audit with Another Accounting Firm*, in [PCAOB Release 2022-002](#) when dealing with referred-to auditors. 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. In the PCAOB's proposed standard, there are inquiries of, and representations from, the referred-to auditor, however, 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. (PwC)
- The commenter questions whether 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. (PwC)
- The construct of the standard results 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. The commenter believes that the ASB could seek to reduce the degree of duplication between a number of requirements, specifically in relation to independence and relevant ethical requirements, offers some drafting suggestions in Appendix 2 of its comment letter, but believes there may be further opportunities to streamline. (PwC)

The following are other concerns and suggestions included in 3 comment letters in response to question 11:

- With regard to the consideration of competencies [of referred-to-auditors], the first bullet of par. A168 is a self-certification from the referred-to auditor, which is meaningful evidence of their competency. We recommend that A167-A168 take the approach of evaluating the presentation and disclosure of the financial statements and identification of information in the component financial statements that contradicts audit evidence or accounting positions from the group financial statements as the other primary considerations of evaluating competences. Absent such errors and contradictions, group auditors often don't have sufficient evidence to evaluate competencies as currently outlined in the standard. Additionally, paragraph 52, as written, "When making reference to the audit of a referred-to auditor, the group engagement partner should take responsibility for determining that referred-to auditors have the appropriate competence and capabilities" seems to indicate that the group auditor is taking more responsibility than suggested in the application guidance. The commenter recommends that this language be modified to clarify the responsibility. The following is a suggested modification, "When making reference to the audit of a referred-to auditor, the group engagement partner should ~~take responsibility for use~~ judgement to determine whether there is any contrary evidence that referred-to auditors have the appropriate competence and capabilities". As discussed above, contrary evidence would be material errors or omissions observed in the financial statements, contradictory information and evidence between the component and group financial statements, and deficiencies reported in the peer review report. (Eide Bailly)
- Paragraph 52 of the ED is in the context of the group engagement partner taking responsibility for determining that referred-to auditors have the appropriate competence and capabilities. However, paragraph 28a of the ED, which relates to component auditors, is written as "the group engagement partner should determine..." It is unclear why the group engagement partner can assign responsibility for this action with regard to referred-to auditors but not component auditors. The commenter asks the ASB to reconsider these requirements and whether it would be more appropriate for them to be consistent. (GT)
- If it is the intent of the Board for group auditors to have a substantial responsibility in determining that the referred-to auditor has the appropriate competency and capabilities, paragraph 52 should provide more definitive guidance on the types of evidence required to be obtained. (Eide Bailly)
- To enhance the clarity and understandability of the requirements related to referred-to auditors the commenter proposes the following revisions:

Eliminate the lead-ins of proposed paragraphs 51, 52, and 54, since the auditor needs to execute on these requirements before making the decision to make reference to a referred-to auditor (such determination is addressed in proposed paragraph 55). We found the lead-ins confusing given the flow of the requirements. We believe that the headings and subheadings are sufficient to guide auditors to understand which requirements relate to making reference to referred-to auditors such that the lead-ins are unnecessary.

In order to enhance the understandability of the requirement, revise the first sub-bullet of proposed paragraph 51 as follows:

~~Referred-to auditors having been made aware of~~ **Communicating to referred-to auditors the** relevant ethical requirements that are applicable given the nature and circumstances of the group audit engagement

For consistency, a similar revision should be made to the similar requirement for component auditors in proposed paragraph 27a.

Flip the order of bullets (a) and (b) in paragraph 63 of the ED to align with the ordering in the corresponding requirements related to component auditors. (GT)

- The commenter has concerns as to how the “communications with the referred-to auditor” (paragraphs 62 – 65) requirements will be applied in practice. Given the principles-based approach to the extent of two-way communications between group auditors and referred-to auditors, and our historical experience when involved in engagements with referred-to auditors, we anticipate wide variation in the characteristics of certain two-way communications between group and referred-to auditors which could potentially have negative impacts on audit quality. (Mazars)
- 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). (PwC)

#### **Task Force Response:**

Comment letter responses to question 11 were preliminarily discussed with the ASB during the July 19-21, 2022, meeting as Issue 2: “Practicality of Certain Requirements Related to Referred-to Auditors and Consideration of Alignment with PCAOB Standards.” [Highlights](#) of the July 2022 ASB discussion are included in this discussion memorandum.

Based on the comments received and direction from the ASB, the task force believes the proposed SAS requires limited revisions related to referred-to auditors. The task force considered discussion during the July 19-21, 2022 ASB meeting, including comparing the requirements in the proposed SAS to those in the new PCAOB AS 1206 and acknowledging the PCAOB requirement for a referred-to auditor to be registered with the PCAOB (paragraph .06c of AS 1206). The task force believes this information is required because of the view that PCAOB registration (which results in a firm being subject to PCAOB inspection) by a referred-to auditor provides a certain level of comfort over their qualifications. In contrast, the AICPA has no equivalent registration concept that can be considered. Therefore, the task force believes it is necessary and appropriate for certain aspects of the proposed SAS to differ from AS 1206 (i.e., requirements related to determining competence and capabilities of referred-to auditors and communicating with referred-to auditors), while avoiding unnecessary differences between the requirements related to referred-to auditors in the proposed SAS and AS 1206, which is consistent with the Board’s goals of harmonization with the IAASB. Additionally, since there is no equivalent requirement for registration under the AU-Cs, not being consistent with the PCAOB does not result in “an unnecessary difference”.

The task force has made limited revisions to the proposed SAS related to referred-to auditors (see Agenda Item 2A).

#### Communicating Significant Risks

When considering comments related to Question 11, the Task Force noted that there was one comment related to the requirement in paragraph 62c of the proposed SAS for the group auditor to communicate to the referred-to auditor identified significant risks of the group financial statements, whether due to fraud or error, that are relevant to the work of the referred-to auditor. The task force acknowledges that the Board previously discussed this topic, but is bringing this to the Board’s attention again given the comment received.

History on this topic is as follows:

- **October 2021:** Agenda item 5 (proposed AU-C 600 marked from the IAASB’s September 2021 draft of proposed ISA 600 (Revised)) was distributed to the Board and discussed during the October 12-14, 2021 Board meeting. The October draft did not include a requirement for the group auditor to communicate identified significant risks to the component auditor or referred-to auditor. During the October 2021 Board meeting, the Board discussed the following:

- Paragraph 41d of extant AU-C 600 requires the group engagement team to communicate identified significant risks to the component auditor and referred-to auditor. In contrast, the October 2021 draft, which is based on the September 2021 draft of proposed ISA 600 (Revised), does not include such a requirement.
  - Given the Board's audit quality objectives, it seems inappropriate to remove the requirement in paragraph 41d of extant AU-C 600 paragraph 41d. Consideration should be given to reinstating a requirement for the group auditor to communicate identified significant risks to the component auditor or referred-to auditor.
  - A referred-to auditor's audit may already be in-process or completed prior to the planning/performance of the group audit. Consideration should be given to whether a requirement for the group auditor to communicate identified significant risks to the referred-to auditor would be practical or appropriate when the referred-to auditor's audit is already completed.
- **October 2021 – January 2022:** Based on the Board's direction to the task force, as well as further task force discussion on the topic, the task force reinstated a requirement for the group auditor to communicate identified significant risks to the component auditor or referred-to auditor.
  - **January 2022:** Agenda item 2 (the proposed SAS *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Auditors)* marked from ISA 600 (Revised) that was voted final in December 2021 by the IAASB) was distributed to the Board and discussed during the January 25-27, 2022, ASB meeting. The January draft includes a requirement for the group auditor to communicate identified significant risks of the group financial statements to the component auditor or referred-to auditor. During the January 2022 Board meeting, the Board did not discuss any issues or concerns related to such requirement.
  - **March 2022:** Same status as January 2022. Exposure draft included the requirements noted above.

In light of the comments received through exposure (see PwC comment above), because the ISAs do not address this area (because the ISAs do not address making reference), and in order to eliminate unnecessary differences with the PCAOB standards, the task force would like to revisit this topic with the Board and has the following question for the Board.

For ease of reference, the requirement in paragraphs 62c of the ED (and newly added application material paragraph A182A) are as follows:

*Communications With the Referred-to Auditor* (Ref: par. **Error! Reference source not found.–Error! Reference source not found.**)

**62.** The group auditor should communicate the following to a referred-to auditor on a timely basis:

...

- c. Identified significant risks of the group financial statements, whether due to fraud or error, that are relevant to the work of the referred-to auditor

...

*Communications With the Referred-to Auditor* (Ref: par. 0–**Error! Reference source not found.**)

**A182A.** The group auditor and referred-to auditor communicate regarding the matters in paragraphs 62–63 to support the group engagement partner taking overall responsibility for managing and achieving quality on the group audit engagement without the group auditor being involved in the work of the referred-to auditor.

**Question for the ASB:**

3. Paragraph 62c of the proposed SAS requires the group auditor to communicate to the referred-to auditor identified significant risks of the group financial statements, whether due to fraud or error, that are relevant to the work of the referred-to auditor. When considering the history on this topic and comments received through exposure (see above), which of the following options does the Board recommend?

**Option 1 (no changes):**

- Retain the requirement in paragraph 62c of the proposed SAS and
- Retain the application material in paragraph A182A

**Option 2:**

- Retain the requirement in paragraph 62c of the proposed SAS and
- Add an example, such as the following, to paragraph A182A to clarify why communication of identified significant risks to the referred-to auditor is necessary:

*“For example, the group auditor communicates identified significant risks of the group financial statements to the referred-to auditor so that the referred-to auditor is aware of the relevant significant risks as identified by the group auditor and can consider the significant risks in their audit.”*

**Option 3:**

- Remove the requirement in paragraph 62c of the proposed SAS and
- Add an example, such as the following, to paragraph A182A to address more limited circumstances in which the group auditor may communicate identified significant risks to the referred-to auditor:

*“For example, when a referred-to auditor’s audit is not yet completed, the group auditor may communicate identified significant risks of the group financial statements to the referred-to auditor so that the referred-to auditor can consider the significant risks in their audit, as appropriate.”*

**Request for Comment 12: Magnitude of Portion of Financial Statements Audited by Referred-To-Auditor**

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

Explanation: The last sentence of par. A41 of the ED states, “As the magnitude of the portion of the financial statements that is audited by referred-to auditors increases, it is less likely that the group engagement partner can conclude that sufficient appropriate audit evidence can be obtained.”

<b>Question 12:</b> Is the last sentence of paragraph A41 clear?	<b>No. of Responses</b>
Yes	5
Yes with suggestions	1
No	13
No comment	3
No. of comment letters	22

<b>Question 12:</b> Is there additional application material that is needed, and if so, what should it be?	<b>No. of Responses</b>
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OK as is	3
Additions	9
No comment	10
No. of comment letters	22

For ease of reference, the application material in paragraphs A41 of the ED is as follows:

**A41.** There may be more complexities in determining whether sufficient appropriate audit evidence can reasonably be expected to be obtained in a group audit where reference is made to the audit of referred-to auditors in the auditor's report on the group financial statements, including in group audits where no component auditors are also involved. The group engagement partner may consider the nature and extent of work performed by referred-to auditors, including matters such as the following:

- The financial significance of the components that are audited by referred-to auditors
- The risks of material misstatement to the group financial statements associated with the portion of the company's financial statements for which the group auditor or component auditor performs audit procedures compared to the portion audited by referred-to auditors

As the magnitude of the portion of the financial statements that is audited by referred-to auditors increases, it is less likely that the group engagement partner can conclude that sufficient appropriate audit evidence can be obtained.

Thirteen commenters indicate that the last sentence of par. A41 is not clear and provided the following additional comments about that sentence:

- Five commenters found this sentence to be problematic because, in the government auditing environment, it is not uncommon for referred-to auditors to perform a substantial percentage of the audit work. They believe that, if the procedures outlined in paragraphs 51 – 66 related to making reference are adhered to and adequately documented, there is no reason why magnitude alone should imply that sufficient appropriate audit evidence could not be obtained by the group engagement partner. (COV, MI OAG, NSAA, VSCPA, Eide Bailly)
- Two commenters suggested that the ASB add a "Consideration Specific to Governmental Entities" paragraph to address the magnitude concept with relation to opinion units in a governmental environment or expand paragraph A43 to more clearly address magnitude considerations related to opinion units. (COV, MI OAG)
- To avoid diversity in practice, four commenters recommended that a better delineation be made (in numbers or words) to identify where the threshold is for concluding that the group engagement partner cannot make reference to a referred-to auditor. (E&Y, TXCPA, OSCPA, CLA) One commenter suggested that the SAS provide a figure as a starting point in the SAS to help drive consistency in practice and noted that consistency is especially relevant, as this matter involves the coordination of different firms. The commenter recommended that the following language from par. .06A of PCAOB AS 2101, *Audit Planning*, be added: (E&Y)

In addition, in an audit that involves referred-to-auditors, the participation of the engagement partner's firm ordinarily is not sufficient for it to serve as lead auditor if the referred-to-auditors, in aggregate, audit more than 50 percent of the company's assets or revenues.

Commenters requested clarification or application guidance regarding the following matters:

- Certain qualitative factors can be important considerations for determining whether the group auditor can obtain sufficient appropriate audit evidence on which to base an opinion on the group



financial statements. Provide additional considerations for the group engagement partner, such as the location of group operations and group management, and the extent of the group engagement team's knowledge of the overall financial statements and familiarity with the group. (GT)

- Clarify that the group engagement partner's assessment of the magnitude of the portion of the financial statements audited by the referred-to auditor includes quantitative and qualitative (emphasis added) considerations relating to the financial information and disclosures that could reasonably be expected to influence the economic decisions of users of the group financial statements. (BDO)
- To avoid a strictly monetary interpretation of magnitude, add a phrase to the final sentence that incorporates the need to consider the qualitative magnitude of risks vs. solely the quantitative magnitude of the portion of the financial statements audited by the referred-to auditors. (TIC)
- Both extant AU-C section 600 and the first bullet in paragraph A41 of the proposed SAS use the term "financial significance." It is unclear if "magnitude" is intended to have a different meaning from "financial significance" and, if so, what that meaning is. Additional, or revised, application material clarifying the intended meaning of "magnitude" would add to greater understanding of the intent of paragraph A41. (Mazars)
- Clarify whether the considerations in par. A41, including the financial significance of the components and risks of material misstatements to the group financial statements associated with the components, also apply when component auditors are involved. Clarify whether there would ever be an instance where the component audited by a component auditor would be too significant, as determined by various criteria, for the group auditor to obtain sufficient appropriate evidence. (E&Y)

#### Task Force Response:

Comment letter responses to question 12 were preliminarily discussed with the ASB during the July 19-21, 2022, meeting as Issue 3: "Considering the Magnitude of the Portion of the Financial Statements Audited by Referred-to Auditors in Determining Whether Sufficient Appropriate Audit Evidence Can Reasonably be Expected to be Obtained." [Highlights](#) of the July 2022 ASB discussion are included in this discussion memorandum.

Based on the comments received and direction from the ASB, the task force believes that paragraph A41 of the proposed SAS requires revision and has revised paragraph A41 as follows (see Agenda Item 2A):

**A41.** There may be more complexities in determining whether sufficient appropriate audit evidence can reasonably be expected to be obtained in a group audit where reference is made to the audit of referred-to auditors in the auditor's report on the group financial statements, including in group audits where no component auditors are also involved. The group engagement partner may consider the nature and extent of work to be performed by referred-to auditors, including matters such as the following:

- The financial significance of the components ~~that are~~ audited by referred-to auditors
- The magnitude of the portion of the financial statements audited by referred-to auditors
- The risks of material misstatement to the group financial statements associated with the portion of the company's financial statements for which the group auditor or component auditor performs audit procedures compared to the portion audited by referred-to auditors
- The importance to the group of the components audited by referred-to auditors, considering qualitative factors



More complexity in determining whether sufficient appropriate audit evidence can reasonably be expected to be obtained may indicate an area of significant judgment.<sup>35</sup>

~~As the magnitude of the portion of the financial statements that is audited by referred-to auditors increases, it is less likely that the group engagement partner can conclude that sufficient appropriate audit evidence can be obtained.~~

<sup>35</sup> Paragraph A93 of the proposed QM SAS.

**Question for the ASB:**

**4.** To avoid affecting current practice in governmental audits while responding to other concerns raised by commenters, the task force is seeking input from the ASB on the proposed revisions to paragraph A41, including whether the proposed revisions do the following:

- a. Provide necessary flexibility for governmental audits so as to not affect current practice.
- b. Resolve questions raised about the meaning of the term “magnitude.”
- c. Address suggestions for additional qualitative considerations to be added.
- d. Provide sufficient guidance for group auditors to conclude whether sufficient appropriate evidence can be obtained without the need for a quantitative threshold (similar to that of the PCAOB).

**Request for Comment 13: Effective Date**

<b>Question 13.</b> 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?	<b>No. of Responses</b>
Yes	19
No comment	3
No. of comment letters	22

Nineteen commenters believe that the proposed effective date provides 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.

ASB drafting conventions, permit early adoption of a SAS when there is no explicit language that states otherwise. Three of the commenters indicated that they believe early adoption would be beneficial but based on their comments are not aware of this option because it is not stated in the proposed SAS. (RSM, OSCP, TXCPA) There were also a number of comments received (see appendix) related to various independence concerns that potentially would be challenging if not solved prior to early implementation of the proposed SAS (e.g., how the new definition of engagement team would be applied, if the independence requirements related to referred-to auditors is not clarified).

One commenter expects many firms will early adopt to align with the adoption of ISA 600 (Revised) and the IAASB's new and revised quality management standards and notes that implementing a risk-based approach for a group audit would be particularly challenging for initial audits. The commenter strongly encourages the Board to develop transition guidance to help auditors that early adopt the guidance because implementation of this proposal would require significant effort, including potential discussions across global networks, early communication and planning with group management and those charged with governance of the group.

**ASB Meeting Highlights  
July 19-21, 2022**

**Group Audits**

In March 2022, the ASB issued an exposure draft (ED) of a proposed SAS *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Auditors)* that would supersede extant AU-C 600, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)*. The ASB discussed preliminary feedback from the comment letters received on the ED and provided direction on the following matters:

Paragraphs A47–A49 of the ED address obtaining sufficient appropriate evidence when there are restrictions on access to information or people at a component that is accounted for as an equity method investment (EMI). With regard to those paragraphs some ASB members

- believe the proposed SAS should be aligned with Appendix B of PCAOB AS 1105, *Audit Evidence*. If the financial statements have been audited by an auditor whose report is satisfactory for the investor auditor's purposes, the financial statements and report may constitute sufficient appropriate evidence. If additional audit evidence is needed, the group auditor would be required to perform procedures to gather such evidence.
- expressed concern that some auditors may fail to perform procedures beyond obtaining the financial statements of the EMI and the auditor's report, even when additional audit evidence is needed.

With regard to the requirements for determining that referred-to auditors and component auditors of EMI components have the appropriate competence and capabilities, some ASB members requested clarification on the procedures to be performed to obtain information related to the professional reputation of those auditors.

The last sentence of par. A41 of the ED states, "As the magnitude of the portion of the financial statements that is audited by referred-to auditors increases, it is less likely that the group engagement partner can conclude that sufficient appropriate audit evidence can be obtained." With regard to that sentence some ASB members

- expressed a preference for providing an example "bright-line" quantitative threshold within application material that the group engagement partner can use to make this determination, as is the case in new paragraph .06A of PCAOB AS 2101 *Audit Planning*, where the threshold is 50%.
  - objected to this sentence because in governmental audits a substantial portion of the work is performed by other auditors. Ms. Burzenski, Chair of the Group Audits Task Force, indicated that the ED does not intend to change practice in the governmental area and that the TF will clarify this in the next draft.
- In February 2022, the IESBA released the ED *Proposed Revisions to the Code Relating to the Definition of Engagement Team and Group Audits* (IESBA ED), with proposed revisions to the International Code of Ethics for Professional Accountants (the IESBA Code). The proposed revisions establish provisions that comprehensively address independence considerations for firms and individuals involved in an engagement to perform an audit of group financial statements. The ASB strongly recommended that members of the ASB and PEEC coordinate in their consideration of how such changes could affect the group audits ED.

The ASB will more fully consider the comments received on the ED at its October 2022 meeting, with the goal of voting on a final standard in January 2023.

## Appendix: Comments on the Group Audits ED That Would Require Actions Beyond the Charge of the Group Audits Task Force

The following are comments on the ED in which respondents request actions that go beyond the charge of the Group Audits Task Force, for example, requests for further implementation guidance outside of the proposed SAS and recommendations for the ASB to engage with PEEC on related independence items. The task force is identifying these items so that the ASB can determine the appropriate actions to be taken in response to the comments.

Overall Opinion	Commenter	Comment	Response to Comment
<b>1c. Does the proposed SAS result in a group audit that achieves the objectives of the proposed QM SAS?</b>			
Suggestions	PwC	<p>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.</p> <p>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, <i>Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards</i> (referred to in the question as the QM SAS) and the new Statement on Quality Management Standards (SQMS) 1, <i>A Firm's System of Quality Management</i>. 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.</p>	The TF supports the ASB seeking feedback from the Peer Review Board and continued monitoring of questions post-implementation.
Suggestions	PwC	<p>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.</p> <p><i>Implications of changes to the definition of engagement team with respect to independence and</i></p>	The TF supports the ASB engaging with PEEC on this independence matter. The TF supports PEEC considering undertaking a project to revise the AICPA Code of Professional Conduct in a similar manner to the IESBA

Overall Opinion	Commenter	Comment	Response to Comment
		<p><i>ethics in a group audit</i></p> <p>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.</p> <p>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),<sup>2</sup> 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.</p> <p><i>Considerations relating to sharing audit evidence across the group</i></p> <p>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</p>	<p>project. The TF believes it is important to consider the impact of the IESBA project on the proposed SAS.</p> <p>The TF supports the ASB considering a separate project to address shared service centers and sharing audit evidence. However, it is not directly related to the audit of group financial statements and therefore do not suggest any</p>

<sup>2</sup> ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

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		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.	changes to the proposed SAS.
<b>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?</b>			
Definition of GFS is unclear	COV	<p>We noted that the clarified SAS removes the link of a group financial statement and components, which broadens the business units that could qualify for group financial statements. Specifically, paragraph A4 states “a single legal entity may be organized with more than one business unit ... when those business units have characteristics such as separate locations, separate management, <b>or</b> separate information systems.” We believe the inclusion of “or” within the guidance is improper in a government environment as many business units have separate locations and separate management that are aggregated into a single legal entity’s financial statements; and, in many cases, we would not expect those to create a group audit scenario.</p> <p>To align with the audit requirements for components throughout the proposed SAS, we conceptually believe it is more logical to define a group as components aggregated through a consolidation process. To assist the auditor in identifying components (or business units) that trigger the group audit requirements, the Board should further clarify the relevant criteria for assessing the extent to which separate locations, management, and information systems represent components (or business units) of a group. The following are questions the Board may consider in providing this guidance:</p> <p><b>Location:</b> Does the mere physical presence of the business unit within a separate building constitute a different location? Does the proximity of the business unit location to the group have any effect on the assessment (i.e., street address, campus, town, county, state, country)?</p> <p><b>Management:</b> In a government environment, authority may be delegated to various levels of management. For example, in producing an Annual Comprehensive Financial Report (ACFR), a Governor may delegate responsibility to an agency to produce the ACFR by aggregating financial information from other agencies. As it relates to aggregated Executive branch agencies, is the Governor and his or her administration considered management, or should consideration also be given to differences in agency-level management?</p> <p><b>Information Systems:</b> Does the significance of information systems to the financial statements (i.e., the general ledger) affect the assessment of the group? For example, if a business unit uses the same general ledger system as the group, but uses its own</p>	For government audit guidance, the TF recommends the board revisit the Audit and Accounting Guide <i>State and Local Governments</i> to ensure sufficient guidance is provided in light of this updated standard.

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		capital assets system, does the number of separate systems or materiality of financial amounts within the capital assets system affect the auditor's assessment?	
Definition of GFS is unclear	Eide Bailly	For considerations specific to Government Entities, paragraph 3 of the Exposure Draft references the AICPA Audit and Accounting Guide for <i>State and Local Governments</i> which is a non-authoritative guide. We believe it would be beneficial to expand the application and explanatory material with specific examples for Government entities as opposed to referencing a non-authoritative guide. A common simple example that could be added is when a component unit is blended into a reporting unit. Another very common example is when the aggregate remaining reporting unit includes a number of unrelated activities under the same management, controls, process, and information systems and contrasting when there are disaggregated elements of the reporting unit.	For government audit guidance, the TF recommends the board revisit the Audit and Accounting Guide <i>State and Local Governments</i> to ensure sufficient guidance is provided in light of this updated standard.
Scope and applicability are unclear	MI OAG	We suggest the Board consider going beyond paragraph 3's reference to the Audit and Accounting Guide for State and Local Governments and add a section of "Considerations Specific to Governmental Entities", similar to other AU-C sections. These considerations would address group audits of governmental component units.	The TF recommends the board revisit the Audit and Accounting Guide <i>State and Local Governments</i> to ensure sufficient guidance is provided in light of this updated standard.
<b>4a. 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>			
Yes, with suggestions	Mazars	Yes, we believe that the emphasis on an auditor's professional judgement makes the proposed standard scalable to different sizes and complexities of groups. However, we are concerned that the lack of guidance on how to determine the extent of work to be performed on components will lead to diversity in practice. We recommend that the development of implementation guidance be considered related to scoping by component.	The TF is supportive of future development of implementation guidance in this area.
<b>5b. Do you agree with the application material in paragraphs A203–A219 of the proposed SAS relating to the group auditor's audit documentation?</b>			
Yes, with suggestions	CLA	We agree with the application material in paragraphs A203-A219 in the proposed SAS. However, we have some concerns about the requirements for the final assembly and retention of a component auditor's documentation. When the retention of component auditor documentation is outside the control of the group auditor, we believe it would be difficult for a firm to design and implement responses to address quality risks relating to the quality objective in proposed SQMS No. 1 paragraph .32f. We suggest the ASB consider enhancing the guidance in A206 of the proposed SAS to indicate that providing specific instructions to the component auditor would normally be a sufficient response to such quality risks.	The TF believes that the combination of guidance in par. 76, A206, A213-A214, and A216-218 is sufficiently clear to provide instructions/guidance for teams on the requirements of final assembly of the audit file and what is required to be kept in the group audit file itself, without the need for

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			<p>Paragraph A205 (which the TF agrees may cause confusion and has therefore deleted.</p> <p>Additionally, the Task Force does not believe the proposed SAS is the appropriate place to interpret SQMS 1; therefore, the TF suggests the ASB consider whether additional guidance (outside of the proposed SAS) is necessary.</p>
<b>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?</b>			
Definition of CA is unclear	COV	We believe there is opportunity to clarify the definition of the terms “component auditor” and “group engagement partner” as it relates to the definition of the term “engagement team.” Paragraph A23 provides that component auditors may be from a group auditor’s firm. Paragraph A28 indicates that there may be joint engagement partners within a group auditor’s firm, but does not define the term “joint engagement partner.” When a group and its components are audited by different audit teams within the same firm and each audit team is supervised by a partner (or partner equivalent) under the same firmwide system of quality control, we are unclear on whether the partner responsible for auditing a component is a joint engagement partner or a component auditor.	<p>Given the limited use of joint audits in the U.S., any additional guidance related to joint audits would be better placed outside of the proposed SAS, if it’s determined to be needed by the ASB.</p> <p>Additionally, A28 is clarifying that this proposed SAS doesn’t address joint audits. Joint audits are not commonplace in the U.S., and therefore information on how they are conducted and the roles that partners play, does not exist. The TF suggests the ASB consider whether additional guidance related to joint audits (outside of the proposed SAS) is necessary.</p>
Definition of CA is unclear	NSAA MI OAG	We believe the SAS should include a definition of “joint engagement partner” which is referenced in paragraph A28. In group audits where different components are audited by separate audit teams within the same firm under the direction of separate partners or partner equivalents we are	The TF discussed whether the standard should include additional guidance related to



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		unclear as to whether these partners are “joint engagement partners” or “component auditors.”	<p>joint audits and concluded that this topic would be better placed outside of the proposed SAS, if it’s determined to be needed by the ASB.</p> <p>A28 is clarifying that this proposed SAS doesn’t address joint audits. Joint audits are not commonplace in the U.S., and therefore information on how they are conducted and the roles that partners play, does not exist. The TF suggests the ASB consider whether additional guidance related to joint audits (outside of the proposed SAS) is necessary.</p>
Definition of GA is unclear	COV	We are concerned with the wording from paragraphs 16 and A85 that, “the group auditor is responsible for directing and supervising the component auditors and review of their work.” We believe clarification should be added to identify what would constitute as directing and supervising the component auditors and reviewing their work. For example, when auditing the ACFR, does this imply the engagement partner must directly supervise and review all state audits? We feel this is not practical or efficient when other engagement partners are already supervising and reviewing those projects under the same firmwide system of quality control.	The TF points the respondent to SAS 146 (formerly the proposed QM SAS) A86-189 which outlines what direction, supervision, and review entail. For specific government considerations, we refer to the AICPA Audit and Accounting Guide <i>State and Local Governments</i> , for consideration if this matter needs to be addressed.
Definition of GA is unclear	NSAA MI OAG	<p>We are concerned with the language of paragraph 16 and A85 which states, “the group auditor is responsible for directing and supervising the component auditors and review of their work.”</p> <p>Specifically, in the case of a group audit of a state’s ACFR performed by the same firm, does this guidance require that the engagement partner directly supervise all component auditors within the same firm? This is not efficient and is impractical given the engagement partner and component auditors will be operating under the same firmwide system of quality control.</p>	The TF points the respondent to SAS 146 A86-189 which outlines what direction, supervision, and review entail. The changes suggested are not consistent with the principles of the proposed

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		<p>We recommend broadening the definition of group auditor found in paragraph 16 to read (insertions italicized):</p> <p>The <i>firm comprised of the group engagement partner and members of the engagement team, including those component auditors who are within that same firm and follow the same system of quality control as the group engagement partner. The group auditor excludes all other than component auditors.</i></p> <p>If this change is made, additional edits would be needed for paragraph A23 (insertions italicized with strikeouts).</p> <p>References in this proposed SAS to the engagement team, <i>as defined in QM SAS paragraph 12</i>, include the group auditor and component auditors. Component auditors may be from a network firm, a firm that is not a network firm, or the <i>same firm as the group engagement partner auditor's firm</i> (for example, another office within the group auditor's firm). <i>In the latter case, consideration as to whether the component auditors are part of the group auditor will depend on whether that component audit's engagement team is under the same system of quality control as the group engagement partner.</i></p> <p>If these changes are considered, then the guidance in paragraphs 27 and 28 would need to be updated to include a reference to the group auditor, as appropriate.</p>	<p>SAS, SAS 146 and SQMS 1, as it relates to the definition of engagement team.</p> <p>The TF notes that there seems to be concerns with the inability/impractical nature of the group engagement partner supervising all component auditors, regardless of the firm, for governmental audits. As such, the TF encourages further consideration of additional guidance in the AICPA Audit and Accounting Guide State and Local Governments guide to ensure sufficient guidance is provided.</p>
<b>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?</b>			
<b>9. Are there additional requirements or application material relating to EMIs that are needed in the proposed SAS, and if so, what should they be?</b>			
Additions	EY	<p>Additional application material relating to equity method investments (EMI) would be helpful to address practical challenges in applying ED-600 and proposed 600 SAS to EMIs.</p> <p>We believe that if the ASB decides to finalize its proposal, it would need to provide additional guidance to avoid diversity in practice. That is, we believe more guidance is needed to help auditors understand how to audit EMIs as components under the proposed SAS.</p> <p>We agree that an EMI has characteristics of a component, but we note that an entity accounts for an EMI differently than it accounts for a legal entity, branch or geography under consolidation accounting and makes different disclosures. Specifically, the financial position and results of an EMI are presented in the group financial statements in a note to the financial statements, and the only financial statement line items affected are investment in the EMI and equity in net income of the EMI. We believe this is a significant difference that would warrant different procedures from those performed</p>	<p>The TF added requirements and application material for auditing EMIs that 1) addresses options for using audited investee F/S as audit evidence when access is not restricted and 2) aligns closer to the amended PCAOB AS 1105 Appendix B.</p> <p>The TF directs the commenter to paragraph A131 which already addresses determining</p>

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		<p>for a component that is a legal entity, branch or geography. Notably, we believe the determination of planning materiality and scoping of significant accounts would be different for EMIs.</p> <p>To illustrate, consider a group audit that comprises 12 components, which include 10 consolidated legal entities and two EMIs. In the group financial statements, revenue would include the revenue of the 10 consolidated legal entities. Thus, a misstatement in the revenue of one component would represent a misstatement in the consolidated revenue of the group, but a misstatement in the revenue of one EMI would not affect the consolidated revenue of the group and would only affect the equity in net income account. We believe additional guidance could address diversity in practice regarding the following:</p> <ul style="list-style-type: none"> <li>▶ How the group auditor should consider risks of material misstatement in the underlying EMI financial statements</li> <li>▶ How to identify significant accounts in an EMI component when the significant accounts are consolidated and presented as different significant accounts on the group financial statements (i.e., revenues and expenses of the EMI component are consolidated and presented as the equity in net income)</li> <li>▶ How to determine component materiality for a consolidated component and an EMI component</li> </ul> <p>Practical guidance on how to apply ED-600 to EMIs, specifically as it relates to the above matters, would help drive consistency in practice.</p>	<p>component performance materiality for EMIs (consistent with extant AU-C 600 paragraph A66).</p> <p>The TF notes that the principles within the proposed SAS, as well as AU-C 315R, on identifying and assessing RoMMs are also applicable to EMIs. <i>The TF recommends consideration by the ASB of whether further implementation guidance is needed for the areas identified in this comment.</i></p>
<b>11. Are the specific requirements relating to referred-to auditors clear, appropriate, and easily identifiable within the proposed SAS, including when considering exhibit A?</b>			
No	PwC	<p>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</p>	<p>The TF acknowledges that the PCAOB standard requires a referred-to auditor to be PCAOB registered (AS 1206.06c); such registration is likely foundational to certain PCAOB requirements for making reference. The AICPA does not have a similar "registration" concept. The TF</p>

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		<p>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.</p> <p>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.</p> <p>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.</p> <p>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).</p>	<p>believes the PCAOB registration concept distinguishes PCAOB vs. AICPA requirements for making reference. The TF believes the proposed SAS (e.g., requirements related to determining referred-to auditor competence and communicating with referred-to auditors) is appropriate for non-public companies audited as the AICPA does not have a "registration" concept that would provide a certain level of understanding of the referred-to auditor's qualifications.</p> <p>The TF added paragraph A182A to explain why certain two-way communications between the group auditor and referred-to auditor are necessary to support the group engagement partner maintaining overall responsibility.</p> <p>While the construct of the standard does result in some repetition, the TF believes it is clearest to maintain all requirements related to referred-to auditors within one section of paragraphs. The TF believes any lack of clarity due to repetition is alleviated</p>

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			<p>through Exhibit A.</p> <p>The TF believes it is sufficiently clear, when considering paragraphs 42, A31, and A113, that the group auditor should evaluate different financial reporting periods within the group (regardless of whether a component with a different reporting period is audited by a component auditor or a referred-to auditor) in accordance with the applicable financial reporting framework (e.g., FASB ASC 810). The TF does not believe it is appropriate to elaborate on audit implications or interpretations of the financial reporting framework within the proposed SAS, and suggests the Board consider whether anything additional is necessary outside of the standard.</p>
<b>Application Materials/Guidance</b>			
	Crowe	<p>We note that the extant AU-C section 600 includes the following application guidance: “.A65 Consideration of all components, regardless of whether reference is made in the auditor's report on the group financial statements to the audit of a component auditor, is necessary when determining component materiality to reduce the risk that the aggregate of detected and undetected misstatements in the group financial statements exceeds materiality for the group financial statements as a whole. Determining component materiality is necessary for the group engagement team to determine the overall group audit plan for the components for which the auditor of the group financial statements is not making reference to the component auditor.”</p>	<p>The TF believes it is unnecessary to carry forward language from extant AU-C 600.A65 into the proposed SAS because such application guidance does not include an execution action for auditors. Furthermore, use of “necessary” within application guidance does not follow with</p>

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		<p>We believe similar application guidance should be included in the proposed SAS. While the group auditor is not taking responsibility for the portion of the group for which the group auditor is referring to a referred-to auditor, the group auditor still must consider all components to sufficiently address aggregation risk in the group financial statements and to develop the audit plan for the components for which the group auditor is taking responsibility. Without such guidance, we believe that group auditors may not design and plan their audits to sufficiently reduce the aggregation risk inherent in a group audit.</p> <p>In addition, related to the definition of component in paragraph 16 of the proposed SAS, we believe it would be beneficial to include application guidance to help auditors of employee benefit plans understand scenarios where a plan may have more than one component. The following is suggested language, which we recommend placing after paragraph A22:</p> <p><i>Considerations Specific to Employee Benefit Plans</i> (Ref: par. 16)</p> <p>In audits of employee benefit plans, a component may be a separate legal entity or subsidiary, or part of the plan which operates separately, such as in a plan merger where the merged plans are still being administered separately and the assets of the merged plans are being held in separate trusts.</p>	<p>AICPA drafting conventions.</p> <p>The TF recommends the ASB and EBP Expert Panel consider additional guidance in the <i>Employee Benefit Plans: Audit and Accounting Guide</i> to ensure sufficient guidance is provided.</p>
	EY	<p>We believe there is a risk that without sufficient guidance for the following situations, firms may not apply the requirements consistently:</p> <ul style="list-style-type: none"> <li>• Our understanding is that the “use of the work of another practitioner” in the first sentence of paragraph 33 of AT-C section 105 is not intended to address all situations in which the work of another practitioner is used (for example, a service auditor’s report). We encourage the Board to clarify the distinction between “use of the work of another practitioner” and reliance on another practitioner’s report in this paragraph or in the application paragraph.</li> <li>• We believe the ASB should consider new guidance or clarifications to existing guidance to address how an auditor should apply procedures over attestation reports other than service organization reports. We have observed an increase in the use of other reports as audit evidence and believe guidance is needed in this area.</li> </ul>	<p>The TF will pass this information on to the ASB for their consideration as a separate project (as this goes beyond conforming amendments).</p>
	PwC	We encourage the ASB to consider whether it might be helpful to develop illustrative	The TF is supportive of the

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		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.	ASB considering the development of illustrative interoffice/interfirm reports as non-authoritative guidance to support the standard.
	RSM	We note that the AICPA has issued technical questions and answers (e.g., question .23 of Q&A Section 8800) related to the performance of group audits, which will need to be updated upon the finalization of the proposed SAS.	The TF agrees that AICPA Technical Q&A section 8800 related to group audits will need to be updated.
<b>Requirements</b>			
	Deloitte	In February 2022, the International Ethics Standards Board for Accountants (IESBA) issued an exposure draft, <i>Proposed Revisions to the Code Related to the Definition of Engagement Team and Group Audits</i> , which proposed revisions to the International Code of Ethics for Professional Accountants to take into account changes made to the IAASB's quality management suite of standards and group audits standard, particularly the expansion of the definition of engagement team to include non-network component auditors. We recommend that the Professional Ethics Executive Committee ("PEEC") of the AICPA monitor this IESBA project and undertake its own project to revise the AICPA's Code of Professional Conduct ("the Code") for convergence purposes. As part of considering what changes are needed to the Code, it is important for PEEC to clearly articulate the independence requirements of non-network component auditors and ensure that these independence requirements are focused on relationships with those entities that are more likely to threaten the individual's independence, which may be different from those requirements necessary when a component auditor is from a network firm. Please see the Deloitte Touche Tohmatsu comment letter to the IESBA exposure draft for our detailed thoughts on amendments to the ethics and independence requirements. We also recommend that a PEEC project be undertaken in the near term so that the effective date of the proposed SAS and the effective date of proposed changes to the Code can be aligned as much as possible.	The TF supports the ASB engaging with PEEC on this independence matter. The TF supports PEEC considering undertaking a project to revise the AICPA Code of Professional Conduct in a similar manner to the IESBA project. The TF believes it is important to consider the impact of the IESBA project on the proposed standard.
	KPMG	We included additional comments below related to ethics requirements, including those related to independence, for the Board's consideration. i. The International Ethics Standards Board for Accountants released the Exposure Draft <i>Proposed Revisions to the Code Relating to the Definition of Engagement Team and Group Audits</i> (IESBA ED), with proposed revisions to the International Code of Ethics for Professional Accountants (the IESBA Code). Paragraph A68 of the proposed SAS noted that "when the component auditor is not subject to the AICPA Code of Professional Conduct, compliance by the component auditor with the ethics and independence requirements set forth in the International Federation of Accountants Code of Ethics for Professional Accountants is sufficient to fulfill the component auditor's ethical responsibilities in the group audit". As the proposed SAS allows for	The TF supports the ASB engaging with PEEC on this independence matter. The TF supports PEEC considering undertaking a project to revise the AICPA Code of Professional Conduct in a similar manner to the IESBA project. The TF believes it is important to consider the



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		<p>compliance with the IESBA Code, we recommend the Board to consider the interaction of the IESBA ED and the proposed SAS as it relates to compliance with ethical requirements, including those related to independence, particularly with regard to non-network component auditors involved in a group audit.</p> <p>For example, the IESBA ED includes provisions requiring individuals participating in the group audit (including those from a non-network component audit firm) to be independent of the group and the group's related entities (affiliates). The IESBA ED proposes separate independence requirements applicable to non-network component auditor firms. KPMG International has provided responses to the IESBA ED via a separate comment letter that we attached for your reference (particularly our response to question 4 in Appendix A). If the provisions in the IESBA ED are adopted as proposed, the IESBA Code may include different independence requirements from those outlined in the proposed SAS. We recommend the Board to consider such interaction and provide further guidance as necessary to drive consistent application in practice.</p> <p>ii. We appreciate the conforming amendments outlined in Appendix C of the Exposure Draft. As <i>referred-to auditor</i> is a new term defined in the proposed SAS, we recommend the Board also consider working with the Professional Ethics Executive Committee on conforming amendments to the AICPA Code of Professional Conduct by incorporating referred-to auditor where appropriate (in particular paragraph 0.200.020.03c) when <i>component auditor</i> is currently used.</p>	<p>impact of the IESBA project on the AICPA's independence standards.</p>
<b>Clarification Needed</b>			
	CLA	<p>We recommend the ASB clarify the responsibilities of component auditors when performing audit procedures designed by group auditors from a firm other than the component auditor's firm. Specifically, we recommend the ASB provide additional guidance regarding the nature of the component auditor's engagement and the form of communicating the component auditor's overall findings and conclusions.</p>	<p>The TF believes additional guidance of this nature could be addressed in non-authoritative implementation guidance but should not be included in the proposed SAS (which is principles-based).</p>
	Deloitte	<p>Paragraph A96 of the proposed SAS states that the group engagement partner may become aware of information about noncompliance or suspected noncompliance with law or regulations, and in such circumstances, may have an obligation under relevant ethical requirements, laws, or regulations to communicate the matter to the component auditor. Paragraphs 22-23 of the "Responding to Noncompliance With Laws and Regulations" interpretation of the AICPA Code of Professional Conduct ("the interpretation"), as adopted by PEEC in February 2022, address such relevant ethical requirements:</p> <p><i>.23 If the group audit engagement partner becomes aware of noncompliance or suspected noncompliance in the course of a group audit engagement, including as a result of being informed of such a matter in accordance with paragraph .22, the group</i></p>	<p>The TF supports the ASB engaging with PEEC to clarify whether noncompliance or suspected noncompliance should be communicated to referred-to auditors.</p>



Overall Opinion	Commenter	Comment	Response to Comment
		<p><i>audit engagement partner should, in addition to responding to the matter in the context of the group audit engagement in accordance with the provisions of this section, consider whether the matter may be relevant to one or more components whose financial or other information is subject to procedures performed for purposes of the group audit engagement.</i></p> <p><i>In these circumstances, the group audit engagement partner should take steps to have the noncompliance or suspected noncompliance communicated to those performing work at components where the matter may be relevant, unless prohibited from doing so by law or regulation.</i></p> <p>In considering the interpretation, we acknowledge certain definitional changes in the proposed SAS. The proposed SAS changes the definition of the term component auditor and introduces the term referred-to auditor. The extant AU-C section 600 definition of component auditor includes both (a) an auditor whose work the group engagement partner assumes responsibility for, and (b) an auditor whose work the group engagement partner does not assume responsibility for, and accordingly, makes reference to. The auditor described in (b) is no longer defined as a component auditor in the proposed SAS, and instead, is defined as a referred-to auditor. Definitions are as follows:</p> <p><u>Definitions in Extant AU-C Section 600</u></p> <p><b>Component auditor.</b> <i>An auditor who performs work on the financial information of a component that will be used as audit evidence for the group audit. A component auditor may be part of the group engagement partner’s firm, a network firm of the group engagement partner’s firm, or another firm.</i></p> <p><u>Definitions in the Proposed SAS</u></p> <p><b>Component auditor.</b> <i>An auditor who performs audit work related to a component for purposes of the group audit. A component auditor is a part of the engagement team for a group audit.</i></p> <p><b>Referred-to auditor.</b> <i>An auditor who performs an audit of the financial statements of a component to which the group engagement partner determines to make reference in the auditor’s report on the group financial statements. A referred-to auditor is not a component auditor, and accordingly, is not a part of the engagement team for a group audit.</i></p>	

Overall Opinion	Commenter	Comment	Response to Comment
		<p>We believe the interpretation is unclear as to whether noncompliance or suspected noncompliance should be communicated to referred-to auditors. Moreover, we believe it is uncertain whether PEEC <i>intends</i> for:</p> <ol style="list-style-type: none"> <li>1. The language “components whose financial or other information is subject to procedures performed for purposes of the group audit engagement” in paragraph 23 of the interpretation to mean components that are audited by component auditors and referred-to auditors, or alternatively, only components that are audited by component auditors (as defined in the proposed SAS).</li> <li>2. The language “those performing work at components” in paragraph 23 of the interpretation to mean component auditors and referred-to auditors, or alternatively, only component auditors (as defined in the proposed SAS).</li> </ol> <p>Accordingly, we question whether the guidance in the proposed SAS in paragraph 96 that the group engagement partner may have an obligation to communicate noncompliance or suspected noncompliance to component auditors, but not to referred-to auditors, is correct.</p> <p>It is our belief that this matter needs to be clarified by PEEC (including consideration as to whether amendments are necessary to clarify the interpretation with respect to referred-to auditors), such that the appropriate interpretation can then be included in the proposed SAS, as appropriate. Therefore, we recommend the ASB to engage with PEEC, as outlined below, to clarify PEEC’s intention in the interpretation with respect to referred-to auditors:</p> <ol style="list-style-type: none"> <li>1. We recommend the ASB to confirm that PEEC has a clear understanding of the definitional changes in the proposed SAS (i.e., referred-to auditor and component auditor), including an understanding of the circumstances when the group engagement partner makes reference to the audit of a referred-to auditor in the auditor’s report on the group financial statements.</li> <li>2. We recommend the ASB to confirm whether it is PEEC’s intention for noncompliance or suspected noncompliance to be communicated to (a) only component auditors or (b) both component auditors and referred-to auditors.</li> <li>3. Based on PEEC’s confirmed intention, we recommend the ASB to consider whether revisions to the proposed SAS are necessary to clarify the obligation (or lack thereof) to communicate noncompliance or suspected noncompliance to referred-to auditors in</li> </ol>	

Agenda Item 2 – Group Audits, Discussion Memorandum and Issues

Overall Opinion	Commenter	Comment	Response to Comment
		<p>accordance with the interpretation.</p> <p>While we recommend the ASB to engage with PEEC to resolve this matter, we acknowledge our belief that noncompliance or suspected noncompliance should be communicated to component auditors only and not also to referred-to auditors, given the nature of the group auditor and referred-to auditor's relationship.</p>	
	GT	<p>We continue to have concerns about how the definition of engagement team in SAS 146 will be operationalized, particularly with regard to independence. While we understand this matter is currently with PEEC, it is imperative that the Board collaborate with PEEC as there are broader implications beyond referred-to auditors, as defined by US GAAS. With that in mind, we believe the Board has provided sufficient guidance in the proposed SAS to understand these terms.</p>	<p>The TF supports the ASB engaging with PEEC on this independence matter. The TF supports PEEC considering undertaking a project to revise the AICPA Code of Professional Conduct in a similar manner to the IESBA project. The TF believes it is important to consider the impact of the IESBA project on the AICPA's independence standards.</p>