

ICAS Response to:

IESBA Exposure Draft: 'Proposed Revisions to the Code Relating to the Definition of Engagement Team and Group Audits'

31 May 2022



Introduction

ICAS is a professional body for more over 23,000 world class business men and women who work in the UK and in nearly 100 countries around the world. Our members have all achieved the internationally recognised and respected CA qualification (Chartered Accountant). We are an educator, examiner, regulator, and thought leader.

Almost two thirds of our working membership work in business; many leading some of the UK's and the world's great companies. The others work in accountancy practices ranging from the Big Four in the City to the small practitioner in rural areas of the country.

We currently have around 4,000 students striving to become the next generation of CAs under the tutelage of our expert staff and members. We regulate our members and their firms. We represent our members on a wide range of issues in accountancy, finance and business and seek to influence policy in the UK and globally, always acting in the public interest.

ICAS was created by Royal Charter in 1854. The ICAS Charter requires its Boards to act primarily in the public interest, and our responses to consultations are therefore intended to place the public interest first. Our Charter also requires us to represent our members' views and to protect their interests, but in the rare cases where these are at odds with the public interest, it is the public interest which must be paramount.

The ICAS Ethics Board has considered the IESBA Exposure Draft: 'Proposed Revisions to the Code in relation to the Definition of Engagement Team and Group Audits' and I am pleased to forward its comments.

Any enquiries should be addressed to Ann Buttery, ICAS Head of Ethics.

Key Points

Overall, we are generally supportive of IESBA's proposals outlined in the above Exposure Draft and believe that the new provisions will be beneficial to users of the Code. We suggest below a few amendments which we believe will improve clarity for users of the Code and, on a specific matter, question whether the proposals are sufficiently comprehensive.

Responses to the specific questions

Proposed Revised Definition of Engagement Team

1. Do you agree with the proposed changes to the Code related to the revised definition of ET, including: (see Chapters 1, 4 and 6)

(a) The revised definitions of the terms "engagement team," "audit team," "review team" and "assurance team;" and

(b) The explanatory guidance in paragraphs 400.A – 400.D?

(a) Revised Definitions

We are supportive of the proposed revised definitions of the above terms. We do, however, believe that the proposed wording in the Code, not of the definitions themselves, but specifically of the proposed revised paragraph 400.3, could be clearer. In that respect, we have set out our suggestions below which we believe are clearer.

Paragraph 400.3

Paragraph 400.3 states: “This Part applies to all audit team members, including individuals from a component auditor firm who perform audit work related to a component for purposes of a group audit. Section 405 sets out specific independence provisions applicable in a group audit.”

We appreciate that the IESBA is seeking to highlight the new provisions in relation to component auditors in paragraph 400.3 however we note that this paragraph only mentions some members of the “Audit Team for a group audit” as defined in the Glossary - i.e. “including individuals from a component auditor firm who perform audit work related to a component for purposes of a group audit” - and therefore we believe this might cause some confusion. Users of the Code might reasonably ask does Part A then apply to, for example, an “individual within a component auditor firm outside the group auditor firm’s network who can directly influence the outcome of the group audit” who are included within the “Audit team for the group audit” definition?

We note that paragraph 45 of the Explanatory Memorandum clarifies IESBA’s intention by stating the following:

“45. Therefore, given that the expanded definition of ET captures individuals from non-network CA firms and other service providers, the IESBA is proposing a single requirement that all members of the audit team (which includes the ET) for the group audit be independent of the group audit client in accordance with the requirements of Part 4A that are applicable to the audit team (see paragraph R405.3 in Chapter 1).”

We appreciate that it is a challenge to concisely articulate IESBA’s intentions in paragraph 400.3 but, in order to try to avoid users of the Code inadvertently misunderstanding the scope of Part A, we suggest that paragraph 400.3 could say either of the following:

“This Part applies to all audit team members **and, where applicable, the members of the audit team for the group audit, which includes** individuals from a component auditor firm who perform audit work related to a component for purposes of a group audit. Section 405 sets out specific independence provisions applicable in a group audit”.

Or, alternatively:

“This Part applies to all audit team members. In a group audit context, this includes individuals from a component auditor firm who perform audit work related to a component for purposes of a group audit and others within such a firm who can directly influence the outcome of the group audit.”

(b) Comments on Explanatory Guidance

(i) Paragraphs 400.A to 400.D – “Engagement Team and Audit Team”

We note that this section is entitled “Engagement Team and Audit Team” and, whilst “Engagement Team” is essentially defined in paragraph 400.A, “Audit Team” is not defined. Given the purpose of these paragraphs appears to be to provide explanatory guidance, and to make it explicit who is a member of the Engagement Team versus the Audit Team, we suggest it would be easier for users to also include the definition of “Audit Team” within these paragraphs to provide context.

We appreciate that this point may not be as applicable for those using the eCode, as they will be able to access the definitions more easily, but it could be more difficult for those who are not using the eCode and would therefore have to refer back and forth to the definitions in the Glossary in conjunction with these paragraphs. The Code should be self-explanatory and users should easily be able to understand what is required of them.

(ii) Paragraph 400.A - Engagement Team

We note that the definition of Engagement Team in the Glossary is as follows:

“An engagement team includes all partners and staff performing the engagement, and any other individuals who perform procedures on the engagement, excluding external experts and internal auditors who provide direct assistance on the engagement. In Part 4A, the term “engagement team” refers to individuals performing audit or review procedures on the audit or review engagement, respectively. This term is further described in paragraph 400.A.”

Paragraph 400.A provides more detailed information about “any other individuals who perform procedures on the engagement” however it does not mention that this excludes “external experts and internal auditors who provide direct assistance on the engagement” as per the definition of “Engagement Team” in the Glossary. In addition, Paragraph 400.C then goes on to discuss “experts” without any context having been provided in the previous paragraphs. For consistency and context, we therefore suggest the following amendments to paragraph 400.A:

“400.A An engagement team **for an audit engagement** includes all partners and staff in the firm who perform audit procedures on the engagement, and any other individuals who perform such procedures who are from:

- (a) A network firm; or
- (b) A firm that is not a network firm, or another service provider.

For example, an individual from a component auditor firm who performs audit work on the financial information of a component for purposes of a group audit is a member of the engagement team for the group audit.

External experts and internal auditors who provide direct assistance on the engagement are not members of the engagement team.”

(iii) Paragraph 400.C - Experts

Definition of External Expert

Paragraph 400.C discusses “Experts”. We note that a “service provider” is defined in proposed paragraph 400.B and believe that there is merit in considering whether the term “external expert” (which is also included within the definition of Engagement Team) should also be defined in the Code of Ethics rather than just referring users to ISA 620 in the Glossary. We note ISA 620 defines “Auditor’s expert” as below:

“Auditor’s expert –An individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the auditor to assist the auditor in obtaining sufficient appropriate audit evidence. An auditor’s expert may be either an auditor’s internal expert (who is a partner or staff, including temporary staff, of the auditor’s firm or a network firm), or an auditor’s external expert. (Ref: Para. A1–A3)”

Experts from a component auditor firm

We also note that whilst there is mention of “experts from a component auditor firm” in the introduction to paragraph 400.C, there is no further mention in the bullet point examples. In particular, the second bullet just mentions “individuals within or engaged by the firm” whilst the definition of “Audit Team for the Group Audit” also includes individuals in such circumstances. Could the bullet point examples be expanded to try to incorporate a component auditor firm situation which would also reflect the Glossary definition? For example, the second bullet could be amended to the following:

“Individuals within or engaged by the firm, **or the component auditor firm**, who have direct influence over the outcome of the audit engagement through consultation regarding technical or industry-specific issues, transactions or events for the engagement are audit team members but not engagement team members.”

(iv) Paragraph 400.D - Engagement quality review

Paragraphs 32 and 33 of the Explanatory Memorandum state: "...The IESBA noted that the extant definitions of the terms "audit team," "review team," and "assurance team" scope in only EQRs within the firm or the network. In reviewing the extant definitions of those terms, the IESBA agreed that EQRs are individuals identified by the firm to perform engagement quality reviews, and such individuals can be sourced from within or outside the firm or its network..." The IESBA then proposed to incorporate the phrase "or engaged by" to clarify this in the respective definitions.

IESBA is therefore proposing to widen the scope of the definitions in relation EQRs but we believe that paragraph 400.D does not make this clear. We therefore suggest the following alternatives for paragraph 400.D to highlight this:

"400.D If the audit engagement is subject to an engagement quality review, the engagement quality reviewer and any other individuals performing the engagement quality review, **which includes individuals from within or outside the firm or its network**, are audit team members but not engagement team members."

Or, alternatively:

"400.D If the audit engagement is subject to an engagement quality review, the engagement quality reviewer and any other individuals performing the engagement quality review, are audit team members but not engagement team members. **This includes individuals from both within the firm or its network and from a non-network component auditor firm**".

Independence Considerations for Engagement Quality Reviewers

2. Do you agree with the changes to the definitions of "audit team," "review team" and "assurance team" to recognize that EQRs may be sourced from outside a firm and its network (see Chapter 6)?

Yes - we agree with the changes to the definitions of "audit team," "review team" and "assurance team" to recognise that EQRs may be sourced from outside a firm and its network. As noted above, we note that this change in definition could be highlighted in proposed paragraph 400.D.

Independence in a Group Audit Context

3. Do you agree with the proposed new defined terms that are used in Section 405 in addressing independence considerations in a group audit (see Chapters 1 and 6)?

"Audit procedures" versus "Audit work"

We appreciate that the IESBA has gone to some considerable lengths to be as consistent as possible with ISA 220 (Revised) with its proposals in this Exposure Draft. We note that ISA 220 (extract noted below for reference), and proposed paragraph 400.A (noted above), refer to auditors performing "audit procedures" while the new definitions of "Audit team for the group audit", "Component auditor firm" and "Group audit client" (noted below for reference) refer to "audit work" rather than "audit procedures". We therefore suggest that IESBA should consider using the term "audit procedures" rather than "audit work" in these new definitions for consistency with ISA 220.

For reference:

Section 405 – new definitions

"Audit team for the group audit: (a) The engagement team for the group audit, including individuals from component auditor firms who perform audit work related to components for purposes of the group audit;

Component auditor firm: The firm performing audit work related to a component for purposes of the group audit

Group audit client: The entity on whose group financial statements the group auditor firm conducts an audit engagement. The group audit client includes its related entities as specified in paragraph R400.20 and any other components that are subject to audit work.”

Extract from ISA 220

“A16. The definition of an engagement team focuses on individuals who perform audit procedures on the audit engagement.

A17. Engagement teams include personnel and may also include other individuals who perform audit procedures who are from: (a) A network firm; or (b) A firm that is not a network firm, or another service provider. For example, an individual from another firm may perform audit procedures on the financial information of a component in a group audit engagement, attend a physical inventory count or inspect physical fixed assets at a remote location.”

4. In relation to the proposals in Section 405 (Chapter 1), do you agree with the principles the IESBA is proposing for:

(a) Independence in relation to individuals involved in a group audit; and

(b) Independence in relation to firms engaged in a group audit, including CA firms within and outside the GA firm’s network?

Yes – we agree with the principles the IESBA is proposing for:

(a) Independence in relation to individuals involved in a group audit; and

(b) Independence in relation to firms engaged in a group audit, including CA firms within and outside the GA firm’s network. We do, however, have some comments on the proposed wording below in relation to non-network component auditor firms.

(i) Need for increased clarity in paragraph R405.7

The Explanatory Memorandum states in paragraph 50 that the last bullet (noted below) is covered by proposed paragraph R405.7:

“Non-network Component Auditor Firms

50. Taking this into consideration, the IESBA is proposing the following independence principles for non-network CA firms:

• In either situation where the group audit client is a PIE or where it is a non-PIE, the conceptual framework (CF) will apply with respect to all other related entities of the component audit client, based on the “reason to believe” test in the related entity principle in extant paragraph R400.20 of the Code (see paragraph R405.7).”

However, we are not convinced that paragraph R405.7 makes this sufficiently clear and therefore suggest that a reference to paragraph R400.20 in paragraph R405.7 would be helpful to users of the Code.

(ii) Reference to “an interest” and cross reference to R400.20

We also note that the Explanatory Memorandum in paragraph 54 (in relation to financial interests in other entities within the group such as an intermediate holding entity) and paragraph 60 (in relation to all other interests or relationships a non-network CA firm might have with the group audit client) states that application of the conceptual framework as specified in paragraph R405.7 provides the appropriate approach. We therefore suggest that also including reference to “an interest”, as well as cross referring to paragraph R400.20, would help cover the situations described in paragraphs 54 and 60 of the Explanatory Memorandum in paragraph R405.7.

“R405.7 When a component auditor firm outside the group auditor firm’s network knows, or has reason to believe, that **an interest**, relationship or circumstance involving the group audit client is

relevant to the evaluation of the component auditor firm's independence from the component audit client, or the group audit client, the component auditor firm shall include that relationship or circumstance when identifying, evaluating and addressing threats to independence (see also paragraph R400.20).”

5. Concerning non-network CA firms, do you agree with the specific proposals in Section 405 regarding:

(a) Financial interest in the group audit client; and

(b) Loans and guarantees?

- (a) We are supportive of the proposed approach.
- (b) We harbour doubts as to whether the proposed approach is rigorous enough. We believe that there would be merit in extending the proposed prohibition for loans and guarantees to cover those between the non-network CA firm and an intermediate holding entity or any other related entities of the group audit client.

Non-Assurance Services

6. Is the proposed application material relating to a non-network CA firm's provision of NAS to a component audit client in proposed paragraph 405.12 A1 – 405.12 A2 sufficiently clear and appropriate?

Yes – we agree the proposed application material relating to a non-network CA firm's provision of NAS to a component audit client in proposed paragraph 405.12 A1 – 405.12 A2 is sufficiently clear and appropriate.

Changes in Component Auditor Firms

7. Is the proposed application material relating to changes in CA firms during or after the period covered by the group financial statements in proposed paragraph 405.13 A1 – 405.13 A2 sufficiently clear and appropriate?

Yes – we agree the proposed application material relating to changes in CA firms during or after the period covered by the group financial statements in proposed paragraph 405.13 A1 – 405.13 A2 is sufficiently clear and appropriate.

Breach of Independence by a Component Auditor Firm

8. Do you agree with the proposals in Section 405 to address a breach of independence by a CA firm?

Yes - we agree with the proposals in Section 405 to address a breach of independence by a CA firm.

Proposed Consequential and Conforming Amendments

9. Do you agree with the proposed consequential and conforming amendments as detailed in Chapters 2 to 6?

Section 360

We note the proposed changes to paragraph R360.16:

R360.16 Where a professional accountant becomes aware of non-compliance or suspected noncompliance in relation to a component or a legal entity or business unit that is part of a group in either of the following two situations, the accountant shall communicate the matter to the group engagement partner unless prohibited from doing so by law or regulation:

- (a) The accountant ~~is, for purposes of an audit of the group financial statements, requested by the group engagement team to~~ performs audit work ~~on financial information~~ related to a the component ~~for the purposes of the group audit~~; or (b) The accountant is engaged to perform

an audit of the financial statements **of a legal entity or business unit that is part of a group** for purposes other than the group audit, for example, a statutory audit.

This is explained in Paragraph 84 of the Explanatory Memorandum as follows:

“84. The proposed conforming amendments to Section 360 address the provisions that deal with communication of non-compliance or suspected non-compliance with laws and regulations in the context of groups. The amendments are intended to recognize that ISA 600 (Revised) does not limit the definition of a component to a legal entity only but also includes, among others, a business unit. Thus, a professional accountant in public practice may be engaged to perform an audit of financial statements of a business unit that is part of a group. Some of the proposed amendments are also to align with terminology used in ISA 600 (Revised).”

We note that a definition of “component” is included in the Glossary as follows: “An entity, business unit, function or business activity, or some combination thereof, determined by the group auditor for purposes of planning and performing audit procedures in a group audit”.

We therefore believe that by stating at paragraph R360.16 “Where a professional accountant becomes aware of non-compliance or suspected non-compliance in relation to a component **or a legal entity or business unit** that is part of a group...” that this additional wording could lead to some confusion because the definition of component in the Glossary already states that it could be an entity or business unit. Indeed, the sentence including these additional words could be read as implying that a component itself would not be a legal entity or business unit which we do not believe is IESBA’s intention.

If there is a wish to make clear in this paragraph that a component could be a legal entity or business unit that is part of a group we suggest the following could be stated instead:

“R360.16 Where a professional accountant becomes aware of non-compliance or suspected non-compliance in relation to a component, **such as a legal entity or business unit**, that is part of a group...”

Or, alternatively:

“R360.16 Where a professional accountant becomes aware of non-compliance or suspected non-compliance in relation to a component, **including a legal entity or business unit**, that is part of a group...”

We further note that this change in wording is repeated throughout the proposed conforming amendments to Section 360 and may need to be re-considered throughout this Section.

Effective Date

10. Do you support the IESBA’s proposal to align the effective date of the final provisions with the effective date of ISA 600 (Revised) on the assumption that the IESBA will approve the final pronouncement in December 2023?

Whilst in principle we appreciate, and are supportive, of aligning the effective date with ISA 600 (Revised) we do question whether this leaves sufficient time for firms to implement the necessary changes.

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