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Mr. Ken Siong
Program and Senior Director
International Ethics Standards Board for Accountants
International Federation of Accountants
529 5th Avenue
New York, New York 10017
USA

Re: *Proposed Revisions to the Code Relating to the Definition of Engagement Team and Group Audits*

Dear Mr. Siong,

BDO International Limited¹ (BDO) is pleased to have the opportunity to comment on the International Ethics Standards Board for Accountants' (IESBA) Exposure Draft (ED) in respect of ***Proposed Revisions to the Code Relating to the Definition of Engagement Team and Group Audits (the ED)***.

General comments

1. BDO supports the collaboration between the International Auditing and Assurance Standards Board (IAASB) and the IESBA in revising the definition of *Engagement Team* as well as developing Section 405, *Group Audits* (Section 405) and ensuring that the requirements are consistent and capable of interoperation.
2. As an international network of firms providing a range of audit and assurance services to national and transnational groups, BDO welcomes and is generally supportive of the introduction of Section 405 into the IESBA Code in setting out the independence requirements in the context of group audits. We do, however have some concerns, as well as suggestions to clarify the proposed revisions. Refer to our responses to the specific questions for these comments.
3. BDO is of the view that the practical application of certain of the requirements may prove to be difficult and we encourage the IESBA to consider providing practical guidance on Section 405 in the form of application material as well as IESBA Staff Guidance material.

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Responses to Specific Questions

Proposed Revised Definition

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

4. The BDO response letter to ISA 600 (Revised)² highlighted that we had concerns with including component auditors in the revised definition of engagement team set out in the proposed ISA 220 (Revised). Our view was that ED-600 correctly required group auditors to be satisfied with the independence, competence, time, due care, performance, and documentation of component auditors, and that the group auditor should adequately direct, supervise and review the component auditor’s work. We did not believe the group auditor should be expected to force their quality management processes on component auditors that they have no legal jurisdiction over, which is what would be required if the component auditor is part of the engagement team.
5. Notwithstanding our previous concerns articulated in our response letter for ISA 600 (Revised), following finalisation of ISA 600 (Revised) BDO is supportive of the proposed changes to the revised definitions of the terms “engagement team,” “audit team,” “review team” and “assurance team” on the basis that this should enable greater consistency and application between the professional standards issued by the IESBA and IAASB.
6. In light of the proposed changes to the revised definitions, BDO suggest the IESBA considers re-wording 400.1. The new definitions (400.A) rely on the fact that individuals, not firms, “perform” audit procedures, whereas 400.1 says that “professional accountants” (i.e., individuals and firms) “perform” audit and review engagements. There is the potential for confusion in how both the IESBA Code and IAASB’s professional standards could be applied not least because the IAASB’s definition of a professional accountant is only to that of an ‘individual’ and not a firm. Therefore, it would be clearer in 400.1 to state that professional accountants must be “independent from their audit and review clients”.

(b) Explanatory guidance in paragraphs 400.A - 400.D - Distinction between “audit team” and “engagement team”

7. With respect to the explanatory guidance in paragraphs 400.A to 400.D, the need to distinguish between “audit team” and “engagement team” in the IESBA Code is not immediately evident. It appears that the ethics and independence requirements applicable to members of the audit team, and those applicable to the engagement team are the mostly the same, with the only difference identified in section 540, which references to the “engagement team” and not the “audit team”.
8. To this end, BDO suggests that the revised requirements clarify the need to distinguish between the “audit team” and “engagement team” and that paragraph 400.C is an appropriate place for this clarity to be included.

² See [BDO Comment Letter](#) dated 2 October, 2020, page 1, paragraph 5

9. In continuing with the distinction between “audit team” and “engagement team”, BDO questions whether there is a disconnect between the international standards on auditing (ISAs) and the IESBA Code. BDO considered the following:

International Standards on Auditing

- a. ISA 220 (Revised) requires the engagement partner to take responsibility for determining whether the relevant ethical requirements, including those related to independence have been fulfilled (ISA 220 (Revised).21). The related application material references to the requirement contained in ISA 700 (Revised) for the auditor’s report to include a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and that the auditor has fulfilled the auditor’s other ethical responsibilities in accordance with these requirements and states that the steps outlined in paragraph 16 to 21 of ISA 220 (Revised) form the basis for including this statement in the auditor’s report (ISA 220 (Revised). A47). Paragraphs 16 to 21 are focused on the “engagement team”.
- b. ISA 600 (Revised) requires the group engagement partner to take responsibility for component auditors’ awareness, understanding and compliance of the relevant ethical requirements, including independence that are applicable (ISA 600 (Revised).25). These component auditors form part of the “engagement team”.
- c. ISQM 2 which highlights that the purpose of “...an engagement quality review is to provide an objective evaluation of the significant judgments made by the engagement team and the conclusions reach thereon.” Further, ISQM 2 goes on to state explicitly that “...the engagement quality reviewer is not a member of the engagement team.” An engagement quality review is an activity conducted at the engagement level but on behalf of the firm and it is not intended to be an evaluation of whether the entire engagement complies with professional standards and application legal and regulatory requirements, or with the firm’s policies or procedures. By including the engagement quality reviewer as part of the “audit team” there is a danger that the objective nature of the engagement quality review is misconstrued by users of the IESBA Code and by implication engagement quality reviewers are perceived to be members of the engagement team.

The IESBA Code

- a. Proposed paragraph 400.3 of the IESBA Code refers to “audit team members”, resulting in the application of Part 4 being wider than that of the ISAs, which is focused on the members of the “engagement team”. It is not clear who is responsible for ensuring that individuals not part of the “engagement team” but part of the “audit team” have complied with the relevant ethical requirements, including independence.
10. BDO recommends that the IESBA engage the IAASB to clarify the performance obligations or expectations of a group engagement partner, when a non-network component auditor is involved, to demonstrate compliance with paragraphs 16 - 21 of ISA 220 (Revised) and paragraph 25 of ISA 600 (Revised).
11. The ISAs explicitly state who is responsible for ensuring compliance with the relevant ethical requirements, including independence of the “engagement team”. BDO further recommends that the IESBA Code clarify who is responsible for ensuring compliance with the relevant ethical requirements, including independence of the “audit team”.

(b) Explanatory guidance in paragraphs 400.A - 400.D - Considerations relating to ISQM 1

12. ISQM 1 requires the firm to establish quality objectives that address the fulfilment of responsibilities in accordance with the relevant ethical requirements, including those relating to independence of the firm and its personnel as well as others (ISQM 1.29). BDO questions whether there is a gap between the firms and individuals covered by ISQM 1 and the IESBA Code.
13. In expanding on “others”, ISQM 1 lists the network, network firms, individuals in the network or network firms, or service providers. It therefore appears that this requirement is aimed at component auditors within the group auditor firm’s network. The significant changes proposed in section 405, *Group Audits* (Section 405) relates to component auditors outside of the group auditor firm’s network, yet the quality objectives contained in ISQM 1 do not seem to address these firms and individuals.
14. BDO recommends that the IESBA engage the IAASB in addressing any gaps in application of ISQM 1 to the component auditor firms outside the group auditor firm’s network, as well as component auditor individuals outside the group auditor firm’s network. Providing further guidance by way of group examples (with network and non-network firms being used as component auditors) would be very helpful to address these gaps.

(b) Explanatory guidance in paragraphs 400.A - 400.D - Service providers

15. With respect to service providers, the explanatory memorandum (EM) to the ED states that the IESBA is proposing to make it explicit that the International Independence Standards (IIS) apply to individuals from service providers who perform audit procedures on an audit engagement, with reference then being made to paragraphs 400.A and 400.B (paragraph 30). The EM then continues to state that it would be disproportionate to bring the service provider’s organization into the scope of the IIS (paragraph 31).
16. Although reference is made to ISQM 1, paragraph 400.B specifically mentions that a service provider includes an individual or organization, creating the impression that the IIS apply to individuals from service providers who perform audit procedures on an audit engagement as well as the service provider’s organization.
17. BDO’s view is that the intention for the IESBA Code to explicitly state that the IIS apply to individuals from service providers who perform audit procedures on an audit engagement has not been achieved and this has the potential to impact on application of IESBA Code by practitioners as well as understanding by those charged with governance and management of group engagements.

Independence Considerations for Engagement Quality Reviewers (EQ 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)?

18. BDO is supportive of the changes to the definitions of “audit team,” “review team” and “assurance team” to recognize that EQ Reviewers may be sourced from outside a firm and its network.
19. As outlined in paragraphs 9 to 11 above, since the EQ Reviewer is a member of the “audit team”, it is not clear who is ultimately responsible for ensuring that the EQ Reviewers comply with the relevant ethical requirements, including independence.

ISQM 2 indicates that it is for the firm to establish policies or procedures that set forth the criteria for eligibility of individuals to be appointed as an EQ Reviewer and that these criteria must include compliance with relevant ethical requirements (including in relation to objectivity and independence of the EQ Reviewer)³. It would be helpful for the IESBA to provide additional practical guidance to highlight the distinction between the various responsibilities of the group engagement partner and the (group) audit firm when determining ‘who’ within the “audit team” has complied with relevant ethical requirements.

20. BDO also encourages the IESBA to provide practical guidance on how firms should be monitoring compliance by an EQ Reviewer outside of the group auditor’s immediate network of firms as this may give rise to practical challenges - not least when a component audit firm is subject to an engagement quality review and that component firm has itself sourced an engagement quality reviewer from outside their own firm or network. This has the potential to place the group engagement team (and their firm) with a near impossible set of circumstances in order to determine compliance with relevant ethical requirements.
21. Given the increased use of assistant EQ Reviewers - particularly as group entity structures continue to evolve - it would also be helpful for the group’s section of the IESBA Code to explicitly reference whether or not the requirements placed on EQ Reviewers as part of the “audit team” also apply to assistant EQ Reviewers.

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)?

22. BDO agrees with the proposed new defined terms that are used in Section 405, with the exception of “Audit team for the group audit”, as explained below.
23. With respect to part (d) of the proposed definition of “audit team for the group audit”, note 2 to paragraph 40 of the EM recognises it will be rare in practice for individuals within a non-network component auditor firm to be able to directly influence the outcome of the group audit if they are not otherwise performing audit work at the component. BDO cannot conceive a situation when this will happen in practice and the inclusion of part (d) in the proposed definition may result in misinterpretation and misapplication of this element of the definition.
24. BDO recommends that IESBA deletes part (d) of the proposed definition of “audit team for the group audit”.
25. If the IESBA decides to retain this element, BDO recommends that the IESBA Code provide practical examples of how (d) might be relevant in practice. Component auditors performing audit procedures on behalf of the group engagement team could be performing a spectrum of audit procedures from performance of a single audit procedure through to conducting a full audit. As a result, it will be helpful to explain how users of the IESBA Code should consider the concept of individuals being able to ‘directly influence’ a component auditor based on the nature of the work that is being performed on behalf of the group engagement team rather than automatically scoping them into the ‘audit team for the group audit’ definition.

³ ISQM 2, paragraph 18 (b)

26. Furthermore, it would be helpful to understand in the context of a group engagement when a component auditor has been engaged to perform audit procedures on behalf of the group engagement team:
- a. 'who' the IESBA anticipates will likely be covered by part (d)
 - b. Whether part (d) also covers those individuals within component firms who:
 - i. recommend the compensation of component auditors in connection with performance of the component audit (such as a senior or managing partner of the component firm)
 - ii. provide consultation regarding technical or industry-specific issues, transactions or events which are then used or considered by the group engagement team

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?

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

27. BDO agrees with the principles proposed in Section 405 (Chapter 1) addressing independence in relation to individuals involved in a group audit.

(b) Independence in relation to firms engaged in a group audit

28. BDO agrees that independence in relation to firms engaged in a group audit needs to be addressed, however how this will be practically implemented and monitored is not clear.
29. Furthermore, the need for the group engagement partner to understand the different audit methodologies across firms that do not form part of the same network will reduce audit efficiencies and increase the costs of a group audit.
30. It will be particularly challenging for the group engagement partner to supervise the work performed by a component auditor firm outside the group auditor firm's network where the group engagement partner has no authority over these individuals and when different audit methodologies are applied.
31. Refer to paragraph 38 for BDO's suggestion relating to practical guidance that will be useful in relation to how group auditor firms monitor financial interests and loans & guarantees held by component auditor firms outside the group auditor firm's network in the group audit client and the extent to which group auditors can rely on the component auditor's ISQM 1 system of quality management

(b) Independence in relation to firms engaged in a group audit- monitoring and evaluating compliance

32. BDO is of the view that the proposed new section lacks clarity and guidance relating to monitoring and evaluation of compliance with the proposed new requirements.

33. To this end, BDO suggests that the IESBA Code explicitly outlines the responsibilities of the component auditor in complying with the relevant ethical requirements and how the group auditor should monitor and evaluate the component auditor's compliance. This should include:
- a. the group auditor's responsibilities in terms of the frequency of monitoring and evaluating the component auditor's compliance with the relevant ethical requirements (i.e., before and during the engagement, as well as prior to the group auditor issuing the group auditor's report),
 - b. the component auditor's responsibilities in relation to the minimum acceptable communication with the group auditor (i.e., before and during the engagement, as well as prior to the group auditor issuing the group auditor's report),
 - c. the group auditor's role in identifying threats relating to the provision of non-assurance services to group audit client or the component audit client,
 - d. the minimum information that the group auditor is required to obtain to evidence the component auditor's compliance, and
 - e. whether the monitoring and evaluation would also extend to the component auditor's use of others (such as EQ Reviewers, service providers).

(b) Independence in relation to firms engaged in a group audit - Key Audit Partner

34. Paragraph 405.11 A1 is proposed as application material to highlight that the group engagement partner might determine that an engagement partner who performs audit work related to a component for the purposes of the group audit is a key audit partner. Our understanding is that this was included as application material instead of a requirement because the group engagement partner applies professional judgment to identify key audit partners from a group perspective based on the facts and circumstances. This may have unintended consequences and result in inconsistent application by group engagement partners.
35. The IESBA Code currently includes a definition for Key Audit Partner and requirements with which the Key Audit Partner must comply. There is no requirement or application material for a specific individual or body to determine who the Key Audit Partners are. Proposed paragraph 405.11 A1 therefore appears to be out of line, in aligning the independence considerations in a group context to the existing requirements of Part 4 of the IESBA Code.
36. To this end, BDO suggests that Section 405 follow the same approach as the extant IESBA Code:
- a. Define a Key Audit Partner from a group audit perspective, and
 - b. Include a requirement for all Key Audit Partners engaged in the group audit and their firms to comply with the requirements set out in paragraphs R411.4 and R524.6, as well as section 540.

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?

37. BDO agrees that the possible threats created by financial interest in the group audit client and loans & guarantees should specifically be considered, however how this will be practically implemented and monitored is not clear.

38. From a practical point of view, BDO encourages the IESBA to provide guidance on how group auditor firms monitor financial interests and loans & guarantees held by component auditor firms outside the group auditor firm's network in the group audit client and the extent to which group auditors can rely on the component auditor's ISQM 1 system of quality management.

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?

Applicability of proposed paragraphs 405.12 A1 - A2

39. The proposed requirement contained in paragraph 405.12 A1 for the component auditor to apply the independence requirements for NAS for PIEs to the component audit client where the group audit entity is a PIE may result in the unintended consequence of increasing market concentration of auditors in reducing the pool of auditors willing to engage with a group auditor firm that is outside of the component auditor firm's network. This could force the group auditor to directly obtain sufficient appropriate audit evidence to support the group audit opinion without engaging with a component auditor firm, resulting in the potential loss of vitally important component auditor knowledge and expertise at the component entity, as well as increased inefficiencies and costs.

40. The group auditor firm develops the group audit plan and determines the work to be performed by the component auditor at component level. The requirement should be proportionate to the self-review threat that is being addressed.

41. To this end, BDO recommends that the IESBA consider a proportionate approach to the prohibition on component auditor firms outside of the group auditor firm's network contained in R405.9 -10 by including consideration of:

- a. the materiality of the component audit client to the group audit client, and
- b. the level of influence that the component auditor firm can exert on the group audit opinion.

Clarity of proposed paragraphs 405.12 A1 - A2

42. Proposed paragraphs 405.12 A1- A2 are not sufficiently clear in outlining that the requirements of Section 600 are applied from the perspective of the component audit client and not the group audit client. The perspective that the requirements are applied from will result in inconsistent applications of the prohibitions and should therefore be clarified.
43. BDO supports the inclusion of examples in the IESBA Code to illustrate the requirements and related application material. Although labelled as examples, the information contained in paragraph 405.12 A1 is a repeat of the requirements and therefore does not achieve the desired effect of illustrating the requirements. Furthermore, the inclusion of these two requirements creates the impression that these are the only two prohibitions that apply and not all those contained in Section 600 of the IESBA Code.
44. To this end, BDO suggests that the examples be removed from proposed paragraph 405.12 A1 and that it will be more useful in this case for the IESBA to develop practical guidance, including Group structures illustrating the application of R405.9 and R405.10 to the related entities from the perspective of the component auditor firm outside of the group auditor firm's network. It will be useful for these examples to illustrate group audit clients that operate internationally, resulting in different local rules being applicable in the different jurisdictions and their interaction with the requirements contained in the IESBA Code.

Transitional arrangements

45. In finalising the proposed revisions, BDO suggests that the IESBA include transitional arrangements to address non-assurance services currently being provided by component auditors that may become prohibited under the revised requirements.

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?

46. BDO is of the view that the proposed application material relating to changes in component auditor firms during or after the period covered by the group financial statements in proposed paragraph 405.13 A1 - 405.13 A2 is sufficiently appropriate.

Breach of Independence

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

47. BDO agrees with the proposals contained in paragraph R405.14 relating to a breach identified by a component auditor firm with the group auditor firm's network.
48. With respect to the proposals relating to a breach identified by a component auditor firm outside the group auditor firm's network, BDO is of the view that a necessary step for the component auditor firm is missing, namely to consider whether, and

appropriately respond to any legal or regulatory requirements. BDO therefore recommends that the following additional step be added as requirement R405.15(e):

In consultation with the group audit engagement partner, the Component Auditor firm shall consider whether any legal or regulatory requirements apply, and if so,

- i. Comply with those requirements, and
 - ii. Consider reporting the breach to a professional or regulatory body or oversight authority if such reporting is common practice or expected in the relevant jurisdiction.
49. With respect to proposed paragraph R405.19, BDO questions why the group audit firm’s communication with those charged with governance is not required to be in writing.
50. While we support the use of visual aids within professional standards, the Illustrative diagram of the proposed process to address breaches of independence at the component auditor firm contained in Appendix 2 is not consistent with the proposed requirements relating to breaches contained in Section 405:
- a. Proposed paragraphs 405.18 A1 and A2 address the group engagement partner’s determination of whether the breach has been satisfactorily addressed by the component auditor or not before determining whether further action is needed, and the breach is communicated with those charged with governance. The illustrative diagram includes an additional step not contained in Section 405 for the group engagement partner to assess the significance of the breach prior to communicating the breach with those charged with governance.
 - b. The illustrative diagram distinguishes between a “significant breach” (block I) and a “very significant breach” (block J), yet proposed section 405 does not include the concept of a “very significant breach”.

Proposed Consequential and Conforming Amendments

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

51. BDO agrees with the proposed consequential and conforming amendments as detailed in Chapters 2 to 6.

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?

52. The revision to the definition of the engagement team in ISA 220 (Revised), making all component auditors part of the engagement team and the resultant implications concerning the application of the IIS in Part 4A of the IESBA Code make it necessary to align the effective date of ISA 600 (Revised) and the IESBA’s final pronouncement.

53. On the assumption that the IESBA will approve the final pronouncement in December 2022 (as indicated in paragraph 92 of the EM), BDO supports the proposal to align the effective date of the final pronouncement with the effective date of ISA 600 (Revised).
54. BDO draws your attention to paragraph 45 of this comment letter for our recommendation for transitional arrangements relating to the proposed non-assurance provisions.

We appreciate the opportunity to comment on the ED, which has proven to be a substantial publication by the IESBA. We hope that our comments and suggestions will be helpful to you in your deliberations and development of future recommendations.

Please contact me should you wish to discuss any of these comments.

Yours sincerely,
BDO International Limited
Chris Smith
Global Head of Audit and Accounting