

**Exposure Draft**  
**February 2022**  
*Comments due: May 31, 2022*

*International Ethics Standards Board  
for Accountants®*

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



International  
Ethics Standards  
Board for Accountants®

## About the IESBA

The [International Ethics Standards Board for Accountants®](#) (IESBA®) is an independent global standard-setting board. The IESBA's mission is to serve the public interest by setting ethics standards, including auditor independence requirements, which seek to raise the bar for ethical conduct and practice for all professional accountants through a robust, globally operable [International Code of Ethics for Professional Accountants \(including International Independence Standards\)](#) (the Code).

The IESBA believes a single set of high-quality ethics standards enhances the quality and consistency of services provided by professional accountants, thus contributing to public trust and confidence in the accountancy profession. The IESBA sets its standards in the public interest with advice from the IESBA Consultative Advisory Group (CAG) and under the oversight of the Public Interest Oversight Board (PIOB).

The structures and processes that support the operations of the IESBA are facilitated by the International Federation of Accountants® (IFAC®).

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## REQUEST FOR COMMENTS

This Exposure Draft, [Proposed Revisions to the Code Relating to the Definition of Engagement Team and Group Audits](#), was developed and approved by the IESBA.\*

The proposals in this Exposure Draft may be modified in light of comments received before being issued in the final pronouncement. Comments are requested by **May 31, 2022**.

Respondents are asked to submit their comments electronically through the IESBA website, using the “[Submit a Comment](#)” link. Please submit comments in both PDF and Word files. Also, please note that first-time users must register to use this feature. All comments will be considered a matter of public record and will ultimately be posted on the website. Although the IESBA prefers that comments are submitted via its website, comments can also be sent to Ken Siong, IESBA Program and Senior Director, at [KenSiong@ethicsboard.org](mailto:KenSiong@ethicsboard.org).

This publication may be downloaded from the IESBA website: [www.ethicsboard.org](http://www.ethicsboard.org). The approved text is published in the English language.

# PROPOSED REVISIONS TO THE CODE RELATING TO THE DEFINITION OF ENGAGEMENT TEAM AND GROUP AUDITS

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## I. Introduction

1. This memorandum provides background to, and an explanation of, the proposed revisions to the *International Code of Ethics for Professional Accountants (including International Independence Standards)* (the Code) relating to the definition of engagement team and the independence requirements in the context of group audits.
2. The IESBA approved these proposed changes for exposure at its [November–December 2021](#) meeting. They are grouped in six chapters in this Exposure Draft.

## II. Background and Overview

### A. Developments Pertaining to the IAASB’s Agenda

#### *Revision of ISA 220*<sup>1</sup>

3. Respondents to the International Auditing and Assurance Standards Board’s (IAASB) December 2015 [Invitation to Comment](#) (ITC), *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits* were supportive of a project to modernize ISA 220. As a result, the IAASB issued the exposure draft [Proposed ISA 220 \(Revised\)](#)<sup>2</sup> (ED-220) in February 2019.
4. Proposed ISA 220 (Revised) was designed to operate (a) as part of the broader quality management system established by the IAASB’s proposed Quality Management standards<sup>3</sup> at both the firm and engagement levels,<sup>4</sup> and (b) in conjunction with ISA 600. Among other matters, ED-220 proposed changing the definition of an engagement team (ET) to recognize different and evolving ET structures, thereby addressing the concerns identified in the ITC.
5. In proposing this definitional change, the IAASB considered that engagement teams may be organized in various ways, including being located together or across different geographic locations or organized by the activity they perform. The IAASB also recognized that individuals involved in the audit engagement may not necessarily be engaged or employed directly by the firm. Thus, the IAASB proposed that they are part of the ET regardless of their location or employment status if the individuals perform audit procedures on the engagement. In this way, their work can be appropriately directed, supervised, and reviewed in accordance with the requirements of ISA 220 (Revised).

#### *Revision of ISA 600*<sup>5</sup>

6. Based on responses to the ITC, other input gathered during related outreach activities, and discussions with the IAASB Consultative Advisory Group (CAG), the IAASB approved a [project proposal](#) to revise ISA 600 in December 2016. The project proposal recognized the strong linkage between the IAASB’s work to clarify and strengthen ISA 600 and the projects to revise other standards,

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<sup>1</sup> ISA 220, *Quality Control for an Audit of Financial Statements*

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

<sup>3</sup> The Quality Management standards are International Standard on Quality Management (ISQM) 1 (Previously ISQC 1), *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*; ISQM 2, *Engagement Quality Reviews*; and ISA 220 (Revised).

<sup>4</sup> See <https://www.iaasb.org/news-events/2019-02/global-consultation-quality-management-firms-and-engagements-now-open>

<sup>5</sup> ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

in particular ISQC 1<sup>6</sup> and ISA 220. As some foundational issues had to be first considered and addressed in these other projects, the IAASB prioritized the progression of these other projects to appropriately build on the revised requirements and application material in making necessary revisions to ISA 600. With progress made on these other projects, the IAASB issued an [Exposure Draft of ISA 600 \(Revised\) \(ED-600\)](#) in April 2020.<sup>7</sup>

7. Respondents to ED-600 raised concerns regarding the interactions of the proposed revised definition of ET with relevant ethical requirements. As a practical matter, given that ED-600 would apply to audits of group financial statements (group audits), the definitional change clarified that component auditors (CAs)<sup>8</sup> (whether in or outside the group auditor firm (GA firm) or its network) are part of the ET for a group audit because they are performing audit work for purposes of the group audit. This raises implications concerning the application of the IIS in Part 4A<sup>9</sup> of the Code.

## **B. IESBA Strategy Consultation**

8. During the IESBA's consultation on its [Strategy and Work Plan 2019–2023](#) (SWP), many stakeholders supported an enhanced level of strategic and technical coordination with other international standard-setting Boards (SSBs), particularly the IAASB, with transparency provided about the work and status of such efforts.
9. Among the SWP consultation paper responses, there was also an encouragement for the IESBA to consider a project to address practical issues encountered by GAs as well as component auditors (CAs) in applying the International Independence Standards (IIS) in the audit of group financial statements. The IESBA determined that it would be appropriate to explore the need for clarifications in this area, but to do so in coordination with the IAASB's project to revise ISA 600.

## **C. Implications of Proposed Revised Definition of Engagement Team for the Code and Related IAASB-IESBA Coordination**

10. The definition of ET in the Code was developed based on the ET definition in extant ISA 220. While the IAASB intended to change the definition in ISA 220 for quality management purposes, the inclusion of CAs in the revised definition raises several questions concerning compliance with the IIS in the context of group audits, given that the definitions of the term in the Code and the ISAs are intended to be aligned. Many respondents to ED-220 requested clarification as to which engagement participants fall within or outside the definitions of "group engagement team" and "component auditor" given different evolving team structures.
11. In the light of the above and following coordination with the IAASB on the ISA 220 project, the IESBA agreed to address the implications of the change in the definition of an ET from the Code's perspective to make clear the independence requirements that apply to the various individuals who are part of the ET under the revised definition. The IAASB, in turn, agreed to make clear in ISA 220

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<sup>6</sup> ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

<sup>7</sup> The IAASB approved ISA 600 (Revised) at its December 2021 meeting. Subject to PIOB approval, the revised standard is expected to be issued in April 2022.

<sup>8</sup> Extant ISA 600 defines a component auditor as "an auditor who, at the request of the group engagement team, performs work on financial information related to a component for the group audit."

<sup>9</sup> Part 4A – Independence for Audit and Review Engagements

(Revised) that the independence requirements applicable to members of the ET are specified in relevant ethical requirements, which, as defined in ISA 220 (Revised),<sup>10</sup> include the Code.

#### **D. Independence of Component Auditors in a Group Audit**

12. A key aspect of extant ISA 600 that intersects with the IIS is the requirement for the group engagement team to obtain an understanding of whether a CA understands and will comply with the ethical requirements relevant to the group audit and, in particular, is independent.<sup>11</sup> Some stakeholders, including firms, have highlighted the need to clarify the meaning of the phrase “ethical requirements that are relevant to the group audit.” This concept is not currently addressed in the Code.
13. Given that CAs outside a firm’s network who perform audit procedures for purposes of a group audit are part of the ET based on the revised definition in ISA 220 (Revised), it is necessary for the IIS to provide clear and consistent guidance concerning the independence of CAs outside the network. Additionally, there is a need to go beyond individuals included in the ET definition and consider the independence framework applicable to the CA firms given that [ISA 600 \(Revised\)](#) establishes a requirement for the group engagement partner (GEP) to take responsibility for confirming whether the CAs understand and will comply with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement.<sup>12</sup>

#### **E. Matters Identified by the IESBA’s Emerging Issues and Outreach Committee (EIOC)**

14. As part of its monitoring of the external environment for emerging issues or developments, the EIOC identified a few matters relating to the application of the IIS with respect to CAs. These include the following:
  - The implications when a parent entity is a public interest entity<sup>13</sup> (PIE), but a component is not, and that component is audited by a non-network firm, particularly whether the CA would need to follow the independence requirements that apply to audits of PIEs or non-PIEs. The Code does not currently address this.
  - The practical implications of a breach of independence at a CA and any safeguards if the GA still intends to use the CA’s work (separately from the GA’s consideration under ISA 600).<sup>14</sup>

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<sup>10</sup> ISA 220 (Revised) was issued in December 2020.

<sup>11</sup> ISA 600, paragraph 19(a)

<sup>12</sup> ISA 600 (Revised), paragraph 25(b)

<sup>13</sup> The extant Code defines a public interest entity as:

(a) A listed entity; or

(b) An entity:

(i) Defined by regulation or legislation as a public interest entity; or

(ii) For which the audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to the audit of listed entities. Such regulation might be promulgated by any relevant regulator, including an audit regulator.

*Other entities might also be considered to be public interest entities, as set out in paragraph 400.8.*

<sup>14</sup> Extant ISA 600, paragraph 20, states the following: “If a component auditor does not meet the independence requirements that are relevant to the group audit, or the group engagement team has serious concerns about the other matters listed in paragraph 19(a)–(c), the group engagement team shall obtain sufficient appropriate audit evidence relating to the financial information of the component without requesting that component auditor to perform work on the financial information of that component.”

**F. Approved Project**

15. Given the above backdrop, in March 2020 the IESBA approved a [project proposal](#) to review the definition of ET and group audits independence considerations in the Code.
16. The objectives of the project are two-fold:
  - (a) To align the definition of the term “engagement team” in the Code with the revised definition of the same term in ISA 220 (Revised) while ensuring that the independence requirements in the IIS are clear and appropriate and apply only to those individuals within the scope of the revised definition who must be independent in the context of the audit engagement; and
  - (b) To revise the IIS so that they are robust, comprehensive, and clear when applied in a group audit context, including with respect to independence for non-network CAs.

**G. Coordination with IAASB**

17. In developing this Exposure Draft, the IESBA has engaged closely with the IAASB to ensure that the proposed changes are consistent and interoperable with the ISAs, especially ISA 220 (Revised) and ISA 600 (Revised). Such close coordination will continue until the completion of this project.

**III. Significant Matters****A. Proposed Revised Definition of Engagement Team**

18. The revised definition of ET in ISA 220 (Revised) includes, among others, CAs and service providers.<sup>15</sup> This raises several questions concerning compliance by these individuals with the IIS in a group audit. Therefore, there is a need to confirm or develop independence requirements applicable to those individuals covered by the extended definition, considering their roles in the audit engagement and the specific facts and circumstances. These matters are further discussed below.
19. In considering aligning the definition of ET in the Code with the definition in ISA 220 (Revised),<sup>16</sup> the IESBA recognized that the extant definition of ET in the Code applies to both audit and other assurance engagements. In contrast, the definition of ET in ISA 220 (Revised) applies only to audit engagements. The IESBA also recognized that the term ET is used in the definitions of the terms “audit team” and “assurance team” in the Code. Therefore, simply substituting the definition of ET in the Code with the revised definition in ISA 220 (Revised) would not be appropriate.
20. While the IESBA accepts that the term ET is used for different purposes in the Code and the ISAs, it is of the view that using the same term in both sets of standards but with different definitions potentially might create confusion among users of the standards, especially given that the Code and the ISAs have historically used the same definition.

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<sup>15</sup> [ISA 220 \(Revised\)](#), paragraphs 12(d) and A17

<sup>16</sup> The revised definition of ET in ISA 220 (Revised) is as follows:

All partners and staff performing the audit engagement, and any other individuals who perform audit procedures on the engagement, excluding an auditor’s external expert<sup>1</sup> and internal auditors who provide direct assistance on an engagement.<sup>2</sup>

(1) ISA 620, *Using the Work of an Auditor’s Expert*, paragraph 6(a), defines the term “auditor’s expert.”

(2) ISA 610 (Revised 2013), *Using the Work of Internal Auditors*, establishes limits on the use of direct assistance. It also acknowledges that the external auditor may be prohibited by law or regulation from obtaining direct assistance from internal auditors. Therefore, the use of direct assistance is restricted to situations where it is permitted.



21. To further inform its deliberations and as part of ongoing coordination with the IAASB, the IESBA considered how ISQM 1 addresses engagement teams for engagements other than audits. Specifically, the term ET as defined in ISQM 1 applies to any team performing procedures on an engagement within the scope of ISQM 1 (i.e., an audit, review, other assurance, or related services engagement). In ISQM 1, the IAASB has established a broader definition of ET, which refers to the performance of procedures on an engagement:
- All partners and staff performing the engagement, and any other individuals who perform procedures on the engagement, excluding an external expert<sup>17</sup> and internal auditors who provide direct assistance on an engagement.
22. In the light of the above, the IESBA is proposing the following to address the alignment of definitions of terms:
- Revise the definition of ET in the Code to align with the definition of ET in ISQM 1, with explanatory guidance to clarify the nature of the various teams in reference to Parts 4A and 4B of the Code (see the proposed revised Glossary in Chapter 6).
  - Making it explicit who is a member of an ET, including an individual from a component auditor firm (CA firm) in a group audit context, and other service providers (see paragraph 400.A in Chapter 1).
  - Use of the term “team” to denote a team of individuals who perform an engagement.
23. The IESBA’s proposals for how the references to the terms “team” and ET would be used in the Code based on the proposed revised definition of ET are set out in Chapter 4.

#### *External Experts*

24. The IESBA acknowledges that the Code currently does not specify independence requirements for external experts. This position mirrored the approach in the extant ISA 220, which, by virtue of the exclusion of external experts from the ET through the definition, did not subject these individuals to the same requirements that apply to ET members. This approach, which the IAASB has retained in ISA 220 (Revised), recognizes that, given the specialized nature of external experts’ work, it would not be appropriate to apply the same level of direction, supervision and review over them as applies to ET members.
25. During the IESBA’s deliberations in developing the revised ET definition, questions were raised (including by the PIOB) as to whether external experts should be subject to independence requirements in audits and other assurance engagements. The IESBA recognized that ISA 620<sup>18</sup> already addresses the auditor’s responsibilities relating to the work of an external expert in obtaining sufficient appropriate audit evidence, including the objectivity,<sup>19</sup> competence, and capabilities of that individual. The IESBA also noted that addressing the matter of independence for external experts is outside the remit of this project. The IESBA nevertheless agreed to consider the matter as part of a future initiative.

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<sup>17</sup> ISA 620, *Using the Work of an Auditor’s Expert*, paragraph 6(a), defines the term “auditor’s expert.”

<sup>18</sup> ISA 620, *Using the Work of an Auditor’s Expert*

<sup>19</sup> ISA 620, paragraph 9, requires that in evaluating the objectivity of an external expert, the auditor makes inquiries about interests and relationships that may create a threat to that expert’s objectivity.

26. Questions were also raised during the IESBA's deliberations regarding whether different types of experts who might be used on an audit engagement are members of the engagement team or the audit team as these terms are defined in the Code. These types of experts include (a) individuals with expertise in a specialized area of accounting or auditing who perform audit procedures, (b) individuals within or engaged by the 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, and (c) individuals who are external experts in fields other than accounting or auditing. The IESBA believes it is in the public interest for there to be clarity in that regard. Accordingly, the IESBA is proposing application material in paragraph 400.C to make clear where these different types of experts stand (see paragraph 400.C in Chapter 1).
27. By the same token, the IESBA is proposing application material to clarify whether an individual performing the engagement quality review is part of the engagement team or audit team (see paragraph 400.D in Chapter 1).

#### *Internal Auditors*

28. Regarding the exclusion of internal auditors who provide direct assistance on an audit engagement when the external auditor complies with ISA 610 (Revised 2013),<sup>20</sup> the IESBA considered whether there would be any change regarding how internal auditors are dealt with in the Code given that the extant Code currently excludes from the ET internal auditors undertaking audit procedures when providing direct assistance on the audit engagement.
29. The IESBA believes that the position in the extant Code continues to be appropriate provided that external auditors appropriately consider the objectivity of internal auditors concerning the work performed. Independence requirements do not apply to internal auditors as the audit client employs or otherwise engages these individuals. Therefore, in revising the definition of ET, the IESBA has retained the position that internal auditors who provide direct assistance on an audit engagement are not part of the ET.

#### *Service Providers*

30. As a result of aligning the proposed definition of ET with the definition of ET in ISQM 1, the IESBA is proposing to make it explicit that the IIS apply to individuals from service providers who perform audit procedures on an audit engagement. The concept of a service provider is defined in ISQM 1.<sup>21</sup> The IESBA proposes to address explicitly service providers' independence, especially those outside a firm's network in the context of group audits, in proposed [Section 405 \(see Chapter 1, including paragraphs 400.A and 400.B\)](#). In substance, however, this would not represent a change in practice because the extant Code already defines individuals *engaged* by the firm or a network firm to perform audit work on the engagement to be part of the ET.
31. Although an individual from a service provider would be covered by the IIS, the IESBA does not believe that the scope of the IIS should be extended to cover the individual's organization (other than in the case of a CA firm outside the GA firm's network, as discussed in Section C below). This is

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<sup>20</sup> ISA 610 (Revised), *Using the Work of Internal Auditors*

<sup>21</sup> ISQM 1 defines a service provider as follows:

An individual or organization external to the firm that provides a resource that is used in the system of quality management or in the performance of engagements. Service providers exclude the firm's network, other network firms or other structures or organizations in the network.

because the individual's organization does not participate in the group audit and is further removed from it. Accordingly, the IESBA considers that it would be disproportionate to bring such an individual's organization into the scope of the IIS.

## **B. Independence Considerations for Engagement Quality Reviewers**

32. During its deliberations, the IESBA noted a matter which required further consideration relating to independence with respect to engagement quality reviewers (EQRs) sourced from outside the firm or the network.<sup>22</sup> 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.
33. 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. This is consistent with ISQM 2.<sup>23</sup> The IESBA believes that EQRs, whose independence plays a vital role in promoting audit quality, should be subject to the same independence requirements regardless of whether they come from within or outside the firm or its network. Similarly, the IESBA believes that individuals who (a) recommend the compensation of, or who provide direct supervisory, management or other oversight of the engagement partner in connection with the performance of the audit engagement, or (b) provide consultation regarding technical or industry-specific issues, transactions or events for the engagement, should be members of the audit team, regardless of whether they come from within the firm. Similar considerations apply with respect to reviews and other assurance engagements.
34. As such, the IESBA proposes to amend the definitions of “audit team,” “review team,” and “assurance team” by adding the phrase “or engaged by” to subparagraph (b) of those definitions to include all such individuals. (Please refer to [Chapter 6 – Glossary of Terms](#) to sight the proposals.)
35. During the development of these proposed revisions, a question was raised as to whether the phrase “engaged by the firm” would suggest that a firm enters into direct contractual engagement with individuals outside the firm rather than the standard practice, which is for firms to be engaging other firms instead of the individuals. The IESBA does not intend the Code to be prescriptive in terms of the manner or type of contract and noted that firms may in some instances contract with individuals directly. The Code must, however, be clear as to which individuals are considered members of the audit team, review team, and assurance team.

## **C. Independence in a Group Audit Context**

36. In thinking through independence considerations in a group audit context, the IESBA approached this matter from two different perspectives:
  - (a) Independence principles for individuals involved in the group audit engagement; and
  - (b) Independence principles for firms, inside and outside of the network, involved in the group audit engagement.
37. To elaborate on these principles, the IESBA is proposing a new Section 405 (Group Audits) and additions of new defined terms to the Glossary as further discussed below.

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<sup>22</sup> ISQM 2 defines an EQR as “a partner, other individual in the firm, or an external individual, appointed by the firm to perform the engagement quality review.” (The definition of “engagement quality control reviewer” in extant ISQC 1 also scopes in an external individual.)

<sup>23</sup> See ISQM 2, paragraph A4

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RELEVANT ETHICAL REQUIREMENTS APPLICABLE TO THE GROUP AUDIT ENGAGEMENT

38. As a starting point, the IESBA believes that it is important to clarify within the context of the Code the meaning of the phrase “relevant ethical requirements, including those related to independence, that apply to the group audit engagement.” This is a concept that is in both the extant ISA 600<sup>24</sup> and ISA 600 (Revised)<sup>25</sup> and it is not explicitly addressed in the extant Code.
39. The IESBA is therefore proposing to make an explicit linkage from the new Section 405 to ISA 600 (Revised) by explaining that (a) Section 405 addresses the relevant independence considerations that apply in a group audit, and (b) the independence requirements referred to in ISA 600 (Revised) (or other relevant auditing standards applicable to group audits that are equivalent to ISA 600 (Revised)) are those specified in that section (see paragraph 405.2 A1).

PROPOSED NEW DEFINED TERMS

40. For purposes of specifying independence provisions for group audits, the IESBA is proposing a set of new defined terms for inclusion in the Glossary to the Code. These terms are as follows:

Term	Definition
<i>Defined Terms Established in ISA 600 (Revised)</i>	
Component	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
Group audit	The audit of group financial statements
Group engagement partner	The engagement partner who is responsible for the group audit
Group financial statements (Note 1)	Financial statements that include the financial information of more than one entity or business unit through a consolidation process
<i>Terms Specific to the Code</i>	
Audit team for the group audit (Note 2)	<p>(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;</p> <p>(b) All others within, or engaged by, the group auditor firm who can directly influence the outcome of the group audit, including:</p> <p>(i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the group engagement partner in</p>

<sup>24</sup> Extant ISA 600, paragraph 19(a)

<sup>25</sup> ISA 600 (Revised), paragraph 25(b), requires the group engagement partner to take responsibility for confirming whether the component auditors understand and will comply with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement.

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Term	Definition
	<p>connection with the performance of the group audit, including those at all successively senior levels above the group engagement partner through to the individual who is the firm's Senior or Managing Partner (Chief Executive or equivalent);</p> <p>(ii) Those who provide consultation regarding technical or industry-specific issues, transactions or events for the group audit; and</p> <p>(iii) Those who perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the group audit;</p> <p>(c) All those within a network firm of the group auditor firm's network who can directly influence the outcome of the group audit; and</p> <p>(d) Any individual within a component auditor firm outside the group auditor firm's network who can directly influence the outcome of the group audit.</p>
Component audit client (Note 3)	<p>When a component is:</p> <p>(a) A legal entity, the entity and any related entities over which the entity has direct or indirect control; or</p> <p>(b) A business unit, function or business activity (or some combination thereof), the legal entity or entities to which the business unit belongs or in which the function or business activity is being performed.</p>
Component auditor firm	The firm performing audit work related to a component for purposes of the group audit
Group	A reporting entity for which group financial statements are prepared
Group audit client (Note 4)	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
Group auditor firm	The firm that expresses the opinion on the group financial statements

## Notes

1. The definition of “group financial statements” in ISA 600 (Revised) elaborates on what a consolidation process includes. Given that this elaboration involves technical accounting concepts such as proportionate consolidation and equity method of accounting, the IESBA does not believe it would be appropriate or necessary to include such a technical elaboration in the definition of the term for purposes of the Code.
  2. The definition of “audit team for the group audit” is based on the definition of audit team but adapted for a group audit. In developing this definition, the IESBA noted that based on the generic definition of audit team, all those within or engaged by the GA firm and all those within the GA firm’s network would be scoped in if they can directly influence the outcome of the group audit. The IESBA considered whether the definition of audit team for the group audit should be extended to include individuals within a non-network CA firm who can directly influence the outcome of the group audit. The IESBA observed that it would be rare in practice for such individuals to be able to directly influence the outcome of the group audit if they are not otherwise performing audit work at a component. Nevertheless, the IESBA is proposing to scope in these individuals within the definition so that they would be captured even if such a situation would be rare (see subparagraph (d) of the proposed definition).
  3. As the definition of a component in ISA 600 (Revised) is not limited to a legal entity but also includes a business unit, function or business activity, or some combination thereof, the IESBA is proposing greater specificity in the definition of a component audit client depending on the nature of the component because the IIS apply only with respect to legal entities:
    - (a) When the component is a legal entity, the component audit client will be the entity itself and any related entities it controls, directly or indirectly. Having regard to the Code’s definition of a related entity, the IESBA believes it would be disproportionate to scope in any other related entities of the entity given that these other related entities are further removed from the audit of the component; or
    - (b) When the component is a business unit, function or business activity (or some combination thereof), the component audit client will be the legal entity or entities to which the business unit belongs or in which the function or business activity is being performed. As above, the IESBA is proposing to take a proportionate approach by not scoping the related entities of such legal entity or entities into the definition. This is because, in practice, control or management of the business unit, function or business activity will rest within the legal entity or entities.
  4. The IESBA is proposing that, as defined, the group audit client includes not only its related entities in accordance with extant paragraph R400.20 of the Code but also any other components that are subject to audit work. This recognizes that the concept of a component in ISA 600 (Revised) extends beyond a legal entity and includes a business unit, function or business activity (or some combination thereof).
41. In proposing these new defined terms to address key concepts in group audits, the project Task Force liaised closely with the IAASB so that these terms and definitions are aligned as closely as possible with those in ISA 600 (Revised). The IESBA also agreed that those new terms and definitions would be best placed in the Glossary and that with the availability of the [eCode](#), they would be visible and readily accessible to users of the Code.

## INDEPENDENCE PRINCIPLES FOR INDIVIDUALS

42. The extant Code addresses the personal independence requirements with respect to an audit client. For a CA firm that belongs to the GA firm's network, individuals from that CA firm who participate in the audit of the component are effectively also required to comply with the same personal independence requirements that apply to the engagement team at the GA firm.<sup>26</sup>
43. The change in the definition of ET in ISA 220 (Revised) results in a need to clarify the independence requirements for individuals at a CA firm outside the GA firm's network and at other service providers. In particular, the IESBA considered whether individuals from non-network CA firms performing work on the component for the group audit should be subject to the same personal independence requirements as individuals from the GA firm and network firms. The IESBA believes that work performed by individuals at CA firms is an important contributor to the group audit, whether the individuals are from CA firms that are network or non-network firms.
44. Accordingly, the IESBA is proposing that the same independence provisions that apply to individuals from the GA firm and CA firms within the network should apply to individuals carrying out audit work at the component level from non-network firms. The IESBA is of the view that the work of the individuals from the non-network CA firms contributes to the audit opinion on the group financial statements just as much as the work performed by individuals from the GA firm and CA firms within the network. This view is aligned with the thrust of the revised ET definition in ISA 220 (Revised), which treats all individuals performing audit procedures on the engagement, whether from within or outside the network, as ET members. This position also applies to individuals from other service provider firms who perform work for the group audit.
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).
46. By taking a consistent approach to personal independence, whether an individual is from a network firm or a non-network firm, the IESBA intends to eliminate any perception that the independence of individuals on the ET outside the GA firm and its network is less important than that of individuals on the ET within GA firm and its network.

## INDEPENDENCE PRINCIPLES FOR FIRMS

47. As a starting point, the IESBA notes that no new principles are required for GA firms or CA firms within the GA firm's network as the extant Code already requires a firm and its network firms to be independent of the audit client. To make this explicit in a group audit context, the IESBA is proposing two requirements in proposed Section 405:
  - With respect to the GA firm, a requirement to be independent of the group audit client in accordance with the requirements of Part 4A that are applicable to the firm (see paragraph R405.4).

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<sup>26</sup> Paragraph R400.51 of the extant Code states the following:

"A network firm shall be independent of the audit clients of the other firms within the network as required."

## EXPLANATORY MEMORANDUM

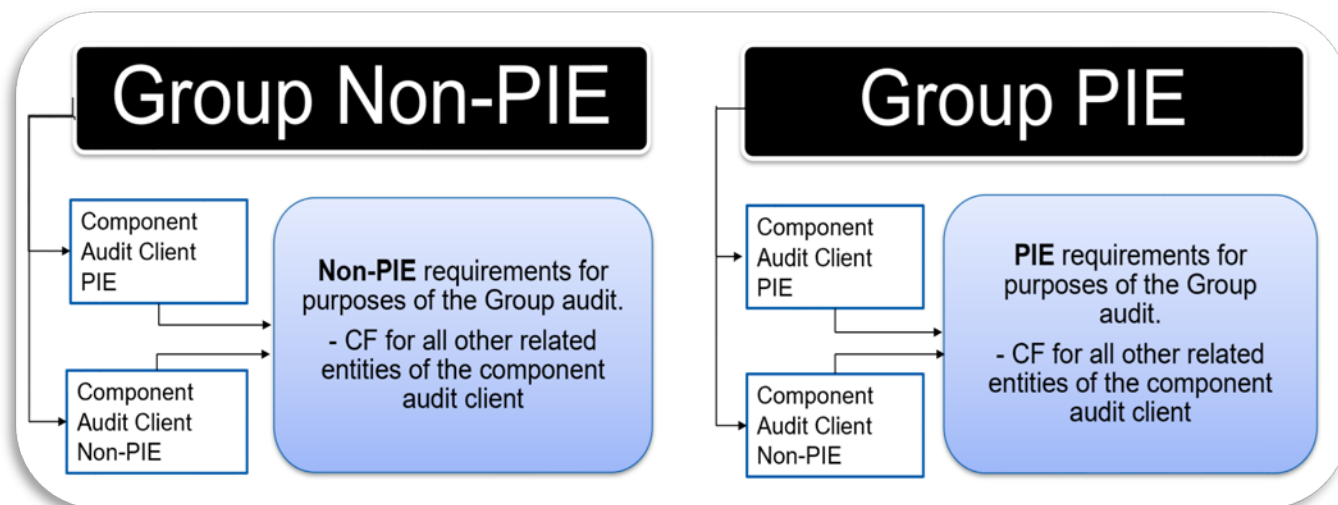
- With respect to network CA firms, a requirement to be independent of the group audit client in accordance with the requirements of Part 4A that are applicable to the network firm (see paragraph R405.5).
48. The key matter the IESBA has then sought to address is to establish principles applicable to firm independence concerning CA firms outside the GA firm's network.

### *Non-network Component Auditor Firms*

49. In deliberating the applicable principles for CA firms outside the GA firm's network, the IESBA considered the approach in the Code that differentiates the independence provisions applicable to PIEs from those applicable to non-PIEs.
50. Taking this into consideration, the IESBA is proposing the following independence principles for non-network CA firms:
- First, the CA firm needs to be independent of the component audit client, consistent with the independence provisions in Part 4A that apply to a firm with respect to all its audit clients (see paragraph R405.6(a)).
  - When the group audit client is a PIE and the component audit client is not itself a PIE, the independence provisions that apply to the CA firm in relation to the component audit client are the PIE provisions (see paragraph R405.10). The IESBA considers that the purpose of the group audit is to report on the group and accordingly, the independence provisions that apply at the group level should apply consistently and uniformly across the group.
  - When the group audit client is a non-PIE, the independence provisions that apply to the CA firm in relation to the component audit client for the purpose of the group audit are the non-PIE provisions regardless of whether the component audit client is a PIE (see paragraph R405.9). As above, the IESBA considers that the focus of the group audit is reporting on the group and therefore the independence provisions that apply at the group level should apply throughout the group.
  - 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).

The diagram below illustrates the latter three principles.





51. Additionally, for all group audit clients, the IESBA is proposing that the same CF approach apply with respect to relationships or circumstances involving *firms within the CA firm's network* with the component audit client or the group audit client, applying the "reason to believe" test (see paragraph R405.8). This recognizes that threats to the CA firm's independence might be created by such relationships or circumstances, and that applying the CF to address such situations represents a more principles-based approach than prescribing specific rules.

#### Financial Interest in the Group Audit Client

52. The IESBA considered whether the Code should more explicitly address certain interests in or relationships with upstream entities as these entities are not captured within the definition of a component audit client. The IESBA noted that the extant Code specifically prohibits a firm and its network firms from holding a direct or material indirect financial interest in an entity that controls the audit client, regardless of whether the audit client is a PIE (paragraph R510.6). Given that financial interests by their nature have the greatest potential to create significant threats and the fact that the work performed by non-network CA firms forms an integral part of the group audit, the IESBA believes that there should be a similar prohibition for non-network CA firms.
53. Accordingly, the IESBA is proposing to introduce an explicit prohibition on non-network CA firms from holding a direct or material indirect financial interest in the entity on whose group financial statements the GA firm expresses an opinion (see paragraph R405.6(b)). Similar to the prohibition in paragraph R510.6 of the extant Code, this proposed prohibition applies to non-network CA firms in respect of both PIE and non-PIE group audit clients. However, unlike extant paragraph R510.6, the IESBA believes there should be no consideration of the materiality of the component audit client to the group audit client. This would achieve a consistent approach relative to the strict prohibition on the GA firm and its network firms from holding a direct or material indirect financial interest in the group audit client pursuant to paragraph R510.4 of the Code.
54. The IESBA considered whether the financial interest prohibition should extend to other entities within the group such as an intermediate holding entity. The IESBA believes the greatest threat lies with respect to the entity on whose group financial statements the GA firm expresses an opinion, hence the proposed prohibition on holding a direct or material indirect financial interest in that entity. The

IESBA believes it may be disproportionate and potentially unduly limit the supply of firms able to act as CA firms if a similar prohibition were to be applied indiscriminately with respect to all other entities within the group. In those other cases, the IESBA believes the application of the CF as specified in paragraph R405.7 provides the appropriate approach to dealing with the threats given the particular facts and circumstances.

#### Loans and Guarantees

55. The IESBA also examined whether other specific interests or relationships should be prohibited explicitly for non-network CA firms with respect to upstream entities.
56. As a result of its deliberations, the IESBA came to the view that loans and guarantees are a further area that should be specifically addressed in the proposed Section 405 (beyond the general application of the CF) because of the financial nature of those relationships. Section 511<sup>27</sup> of the Code addresses loans and guarantees with an audit client. The IESBA considered the scope of application of the prohibitions in Section 511 to a non-network CA firm, specifically whether those prohibitions should apply only with respect to the group audit client or whether they should apply also with respect to related entities of the group audit client.
57. The IESBA first agreed that the prohibitions in Section 511 should apply with respect to the group audit client given that this is the entity on whose group financial statements the GA firm expresses an opinion. The IESBA then considered whether the Section 511 prohibitions should be extended to an intermediate holding entity that controls the component audit client or any other entities within the group that are controlled by the group audit client. There was a view that the level of the threats is no different than in the case of the group audit client given the element of control and accordingly, the prohibitions should apply also with respect to any entity controlled by the group audit client. A related view was that a relationship involving a loan or guarantee that is subject to the specific prohibitions in Section 511 between a firm and an entity within a group for which it acts as a CA firm would be so rare that such a relationship could be questionable and therefore should be prohibited.
58. On the other hand, there were concerns about the potential for unintended consequences in going down a prescriptive path of prohibitions. In particular, there was a practical concern about potentially restricting the pool of non-network firms that could act as CA firms, leading to increased audit market concentration and potential adverse consequences for audit quality. Going down the prescriptive path could result in higher cost for business if they have to engage two firms, one for statutory audit services and another for purposes of the group audit, the result of which is a likelihood that CA firms would be engaged for both services, thereby affecting small and medium practices (SMPs) that often provide statutory audit services. In addition, there was a concern about disproportionate outcomes in some cases if a non-network CA firm performing limited scope audit work for purposes of the group audit were to be subject to a more stringent requirement than when the same firm is performing a full scope statutory audit of the component audit client under the extant IIS.
59. On balance, given those practical concerns, the IESBA considers that the public interest would be better served and the objective of setting proportionate standards better met if the prohibitions in Section 511 on loans and guarantees were to apply only with respect to the group audit client (see paragraph R405.6(c)). For loans and guarantees between the non-network CA firm and an intermediate holding entity or any other related entities of the group audit client, the IESBA believes that the CF provides a robust, principles-based approach to identify, evaluate and address any threats

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<sup>27</sup> Section 511, *Loans and Guarantees*

that might be created in such situations. Indeed, the IESBA noted that depending on the particular facts and circumstances, proper application of the CF may lead to the same outcome as a strict prohibition. The IESBA welcomes stakeholders' views on its proposals on this matter.

#### Other Interests and Relationships

60. With respect to all other interests or relationships a non-network CA firm might have with the group audit client, the IESBA believes the CF should apply using the reason to believe test, consistent with the approach in extant paragraph R400.20 of the Code (see paragraph R405.7).

#### Key Audit Partner (KAP)

61. During its deliberations, the IESBA considered clarifying how the concept of a KAP in the Code applies in the context of a group audit. The KAP concept is used in a few areas of the Code, especially in relation to partner rotation to address long association with an audit client. The extant Code defines a KAP as follows:

The engagement partner, the individual responsible for the engagement quality control review, and other audit partners, if any, on the engagement team who make key decisions or judgments on significant matters with respect to the audit of the financial statements on which the firm will express an opinion. Depending upon the circumstances and the role of the individuals on the audit, "other audit partners" might include, for example, audit partners responsible for significant subsidiaries or divisions.

62. To highlight the relevance and linkage of the KAP concept to a group audit, the IESBA is proposing guidance in Section 405 to explain that a GEP might determine that an engagement partner who performs audit work related to a component for purposes of a group audit is a key audit partner for the group audit because of that individual's role in making key decisions and judgments on significant matters with respect to the audit of the group financial statements. It follows then that once the GEP has communicated that determination to the individual, the individual will be subject to the provisions of the Code that apply to KAPs.
63. Given that the KAP provisions of the Code apply mostly in the context of audits of PIEs, the IESBA is proposing that this guidance be placed within the subsection of Section 405 dealing with group audit clients that are PIEs (see paragraph 405.11 A1).
64. To further strengthen the linkage with ISA 600 (Revised), the IESBA is also proposing an amendment to the definition of a KAP to more explicitly state that other audit partners who make key decisions or judgments on significant matters with respect to the audit engagement might include engagement partners for certain components in a group audit such as significant subsidiaries or divisions (see Chapter 6).

#### Non-Assurance Services (NAS)

65. During its deliberations, the IESBA considered that it would be helpful to clarify the application of the [revised NAS provisions](#) for non-network CA firms in a group audit context, especially given that the NAS revisions have been substantive. Accordingly, the IESBA is proposing guidance in Section 405 to highlight some important considerations when applying the NAS provisions. In the first instance, the IESBA is proposing to make clear that where the group audit client is a PIE, the independence requirements for NAS provided by a non-network CA firm to the component audit client are those applicable for PIEs even if the component audit client is a non-PIE. This is consistent with the overarching principle discussed above that where the group audit client is a PIE, the independence

provisions applicable to the audit of the component audit client are the PIE provisions. The IESBA is proposing that the guidance include some illustrations of this principle in a NAS context (see paragraph 405.12 A1).

66. In addition, the IESBA felt it important to explain how the self-review threat prohibition<sup>28</sup> in the revised NAS provisions should be applied in circumstances where a non-network CA firm performs limited scope work for purposes of the group audit, for example, audit work limited to a specific line item such as inventory. In such circumstances, the reference point for the CA firm in evaluating the self-review threat that might be created by the CA firm's provision of a NAS to the component audit client is the financial information on which the CA firm is performing audit work for purposes of the group audit. Any other financial information of the component audit client is not relevant to the evaluation of that self-review threat because that other financial information is not subject to audit work. (See paragraph 405.12 A2.)

#### **D. Changes in Component Auditor Firms**

67. The IESBA also noted that in practice, there might be circumstances in which the GA firm requests another firm to perform audit work as a CA firm during or after the period covered by the group financial statements. Such circumstances might arise, for example, as a result of an acquisition by the group audit client. To address these types of circumstances, the IESBA is proposing guidance based on the extant provisions of the Code dealing with an entity becoming an audit client during or after the period covered by the financial statements on which a firm will express an opinion.<sup>29</sup> In particular, the proposed guidance explains that a threat to the CA firm's independence might be created by financial or business relationships of the CA firm with the component audit client during or after the period covered by the group financial statements but before the CA firm agrees to perform the audit work, or by previous services provided to the component audit client by the CA firm.
68. Leveraging guidance in the extant Code, the proposed guidance also addresses the situation where a NAS was provided by the CA firm to the component audit client during or after the period covered by the group financial statements, but before the CA firm begins to perform the audit work for the purposes of the group audit, and the NAS would not be permitted during the engagement period.
69. These proposals are reflected in paragraphs 405.13 A1 and A2.
70. In developing the provisions addressing changes in CA firms, the IESBA identified the need for a conforming amendment to paragraph R400.31 of the revised NAS provisions to align subparagraph (b) of that provision to the proposed paragraph 405.13 A1(b). The effect of this proposed conforming amendment to the revised paragraph R400.31 is to not exclude from a firm's consideration any threats to independence created by previous services provided by the firm or a network firm to an audit client during or after the current financial statement period under audit. (See Chapter 3.)

#### **E. Audit of Component Audit Clients for Statutory, Regulatory or Other Reasons**

71. For the avoidance of doubt, the IESBA believes it is important to clarify upfront in the proposed Section 405 that if a CA firm is engaged separately to issue an audit opinion on the financial statements of the component audit client for statutory, regulatory or other reasons, the CA firm might need to comply with independence requirements different from those that would apply for purposes

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<sup>28</sup> Paragraph R600.16 of the revised NAS provisions

<sup>29</sup> Extant paragraph R400.31 and related application material

of the group audit. For example, if the component audit client is a PIE and is subject to a statutory audit, the PIE independence requirements would apply for the statutory audit of the component audit client, even if the group audit client is a non-PIE. (See paragraph 405.2 A2.)

#### **F. Breach of Independence by a Component Auditor Firm**

72. One area that the IESBA believes needs to be clarified in the Code is the process to address a breach of an independence requirement at the CA firm level. The extant Code sets out a process a firm should follow when it concludes that a breach of a requirement of the IIS has occurred. This process is outlined in Appendix 1. If a breach is identified at the GA firm level, the GA firm should follow this process.
73. The IESBA is proposing requirements and guidance in Section 405 to deal with circumstances where a breach is identified at the CA firm level.

##### *CA Firm Within GA Firm's Network*

74. Under the extant Code, a breach of an independence requirement by a network firm effectively is the same as a breach of an independence requirement by the firm and therefore needs to be addressed in the same way, given the requirement for a network firm to be independent of the audit clients of the other firms within the network.
75. To make the linkage to the process to follow under the extant Code in the context of a group audit, the IESBA is proposing that if a CA firm within the GA firm's network concludes that a breach of Section 405 has occurred, the CA firm first communicate the breach immediately to the GEP. The GEP is then required to assess the breach and determine the appropriate actions to take in accordance with the extant provisions of the Code dealing with breaches. (See paragraph R405.14.)

##### *CA Firm Outside GA Firms' Network*

76. One of the practical issues when dealing with CA firms outside the GA firm's network in a group audit context is that it would not be practicable for the GA firm to implement the monitoring and disciplinary procedures necessary to ensure the CA firm's compliance with all applicable independence requirements for the group audit, given that the CA firms are outside the GA firm's control. For this reason, the Code relies on ISA 600 (Revised) to specify the requirements to enable the GA firm to confirm whether the CA firm understand and will comply with the relevant ethical requirements applicable to the group audit, and to receive confirmation from the CA firm that it has complied with those relevant ethical requirements.<sup>30</sup>
77. The independence requirements in a group audit context apply to every member of the ET and include those relating to, for example, financial interests, business relationships, and employment relationships. Many independence requirements also apply to the relevant individuals' immediate and close family members. Thus, while a breach of an independence requirement at the CA firm level could be triggered by any of these individuals, the IESBA is cautious not to imply that the GA firm would automatically not be able to express an opinion on the group financial statements because there has been a breach of an independence provision at a CA firm. For example, the IESBA does not believe that it would be in the public interest to cast doubt on the reliability of all the audit work performed in the group audit if the breach in relation to a component audit client was inadvertent and insignificant. Therefore, a careful consideration of the facts and circumstances of the breach at the

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<sup>30</sup> See, for example, ISA 600 (Revised), paragraphs 25 and 45.

CA firm level is necessary. Further, in the context of the GA firm's ability to use the CA firm's work for purposes of the group audit, the IESBA believes that objectivity is the critical fundamental principle.<sup>31</sup> This is consistent with the focus on the firm's objectivity in the extant provisions of the Code addressing breaches.

78. Given these considerations, the IESBA is proposing that the process to deal with a breach at a non-network CA firm follows broadly similar principles as in the process to deal with a breach in the extant Code (refer to Appendix 2 for a diagrammatic outline). Thus, in the event of a breach at the CA firm level, Section 405 proposes that the CA firm take a number of actions, including communicating the breach promptly to the GEP together with an assessment of the significance of the breach and any actions to address those consequences (see paragraph R405.15). The GEP will then need to assess the breach, focusing on the impact of the breach on the CA firm's objectivity and the GA firm's ability to use the work of the CA firm for purposes of the group audit, before deciding on the need for any further action (see paragraphs R405.16-17).
79. The IESBA is proposing guidance to make clear that in some circumstances, the GEP might determine that additional actions are needed beyond the CA firm's actions to satisfactorily remedy the breach to enable the GA firm to use the CA firm's work (see paragraph 405.18 A1). On the other hand, if the GEP determines that the breach cannot be satisfactorily addressed, the IESBA is proposing guidance consistent with ISA 600 (Revised)<sup>32</sup> to recognize that the GA firm cannot use the CA firm's work. In those circumstances, Section 405 guides the GEP to find other means to obtain the necessary audit evidence on the component audit client's financial information (see paragraph 405.18 A2) to enable the GA firm to express an opinion on the group financial statements.

#### *Communication with Those Charged with Governance (TCWG)*

80. Consistent with the provisions dealing with breaches in the extant Code, the IESBA believes it is necessary to involve TCWG of the group audit client in the process to address a breach at a non-network CA firm. The IESBA is therefore proposing a requirement for the GA firm to communicate with TCWG of the group audit client concerning the breach at a CA firm, including the significance of the breach and whether actions proposed or taken would satisfactorily address the consequences of the breach (see paragraph R405.19).
81. If TCWG do not concur with the GA firm's assessment that the actions proposed or taken satisfactorily address the consequences of the breach, the IESBA is proposing that the Code prohibit the GA firm from using the work of the CA firm for purposes of the group audit (see paragraph R405.20).

#### *Coordination with IAASB*

82. In developing the proposed provisions in Section 405 addressing a breach of independence at a non-network CA firm, the IESBA has engaged in close coordination with the IAASB so as to enable Section 405 and ISA 600 (Revised) to be consistent and interoperable.<sup>33</sup>

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<sup>31</sup> The IESBA would like to emphasize that compliance with the five fundamental principles is the baseline for compliance with the Code. The emphasis on objectivity is to address the ability of the GA firm to use the CA firm's work and, therefore, objectivity is the critical fundamental principle.

<sup>32</sup> See ISA 600 (Revised), paragraph A67.

<sup>33</sup> See, in particular, ISA 600 (Revised), paragraphs A66-A67.

## **G. Other Proposed Consequential and Conforming Amendments to the Code**

83. In addition to the proposed conforming amendments in Chapters 3 and 4 already mentioned above, the IESBA is proposing the following other consequential and conforming amendments:
- (a) Proposed conforming amendments to Section 360 of the Code to align with ISA 600 (Revised) terminology (see Chapter 2); and
  - (b) Proposed consequential amendments to the Code as a result of the finalization of the IAASB's suite of quality management standards<sup>34</sup> (see Chapters 5 and 6).
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).
85. The proposed quality-management related consequential amendments to the Code address a specific matter that arose during the separate project to develop conforming amendments to the Code to align the Code with terms and concepts used in the IAASB's quality management standards.<sup>35</sup>
86. The proposed consequential amendments specify that, in the context of the definitions of "audit team," "review team" and "assurance team," individuals who provide quality control for the engagement under the extant definitions of these terms are those who perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the engagement. The IESBA does not believe it would be appropriate to simply replace the term "quality control" in these definitions with "quality management." This is because under the IAASB's suite of quality management standards, many individuals may be involved in, or perform roles related to, quality management within a firm and it would not be appropriate to indiscriminately scope all of them within the audit team, review team or assurance team. See the proposed amendments to the definitions of "audit team," "review team" and "assurance team" in Chapter 6. Similar amendments are also being proposed to provisions in various sections of the Code that currently refer to individuals providing quality control for an engagement (see Chapter 5).
87. A few other matters were raised during the project to develop quality management-related conforming amendments to the Code. However, these matters are outside the scope of the Engagement Team – Group Audits Independence project and will be considered by the IESBA as part of the development of its future strategy and work plan.

## **IV. Analysis of Overall Impact of the Proposed Changes**

88. The IESBA believes that the proposals are critical to maintaining public trust and confidence in group audits because they aim to respond to questions and concerns that have arisen over a number of years about the application of the IIS in the context of group audits. The enhancements to the Code resulting from this project will serve to further clarify and strengthen the IIS, thereby contributing to public trust and confidence in the quality of the auditor's work.

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<sup>34</sup> ISQM 1, ISQM 2 and ISA 220 (Revised) issued in December 2020

<sup>35</sup> The IESBA approved the quality management-related conforming amendments to the Code at its November-December 2021 meeting.

89. Given the nature and extent of the proposed revisions to the Code, the IESBA believes that some of the proposals may entail significant changes to the policies and methodologies of firms and networks that perform or are otherwise involved in group audits. Such changes may result in increased costs, including with respect to the deployment of updated policies and procedures, and awareness raising and training initiatives.
90. The IESBA also expects costs related to adoption and implementation for national standard setters, professional accountancy organizations and other stakeholders, including translation where needed and education and training efforts. There will also be implications for TCWG potentially in terms of greater interactions with GA firms pursuant to the provisions of the Code addressing a breach of independence at a CA firm.

## V. Project Timetable and Effective Date

91. The IESBA is mindful of the need to coordinate the effective date for the final provisions from this project with the effective date of ISA 600 (Revised).<sup>36</sup>
92. The indicative timeline for the completion of this project is set out below.

Indicative Timing	Milestone
September 2022	<ul style="list-style-type: none"> <li>Discussion of significant matters arising on exposure with IESBA Consultative Advisory Group (CAG)</li> <li>IESBA's full review of respondents' comments and first read of revised proposals</li> </ul>
December 2022	<ul style="list-style-type: none"> <li>IESBA approval of final pronouncement</li> </ul>

## VI. Guide for Respondents

93. The IESBA welcomes comments on all matters addressed in this ED, but especially the matters identified in the Request for Specific Comments below. Comments are most helpful when they refer to specific paragraphs, include the reasons for the comments, and, where appropriate, make specific suggestions for any proposed changes to wording. When a respondent agrees with proposals in this ED, it will be helpful for the IESBA to be made aware of this view.

### Request for Specific Comments

94. The IESBA welcomes comments on the following specific matters. Where a respondent disagrees with a proposal, it will be helpful for the respondent to explain why and to provide suggestions for other ways to address the particular matter.

#### *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

<sup>36</sup> ISA 600 (Revised) will be effective for audits of financial statements for periods beginning on or after December 15, 2023.



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

*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)?

*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)?
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?
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?

*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?

*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?

*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?

*Proposed Consequential and Conforming Amendments*

9. Do you agree 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?

**Request for General Comments**

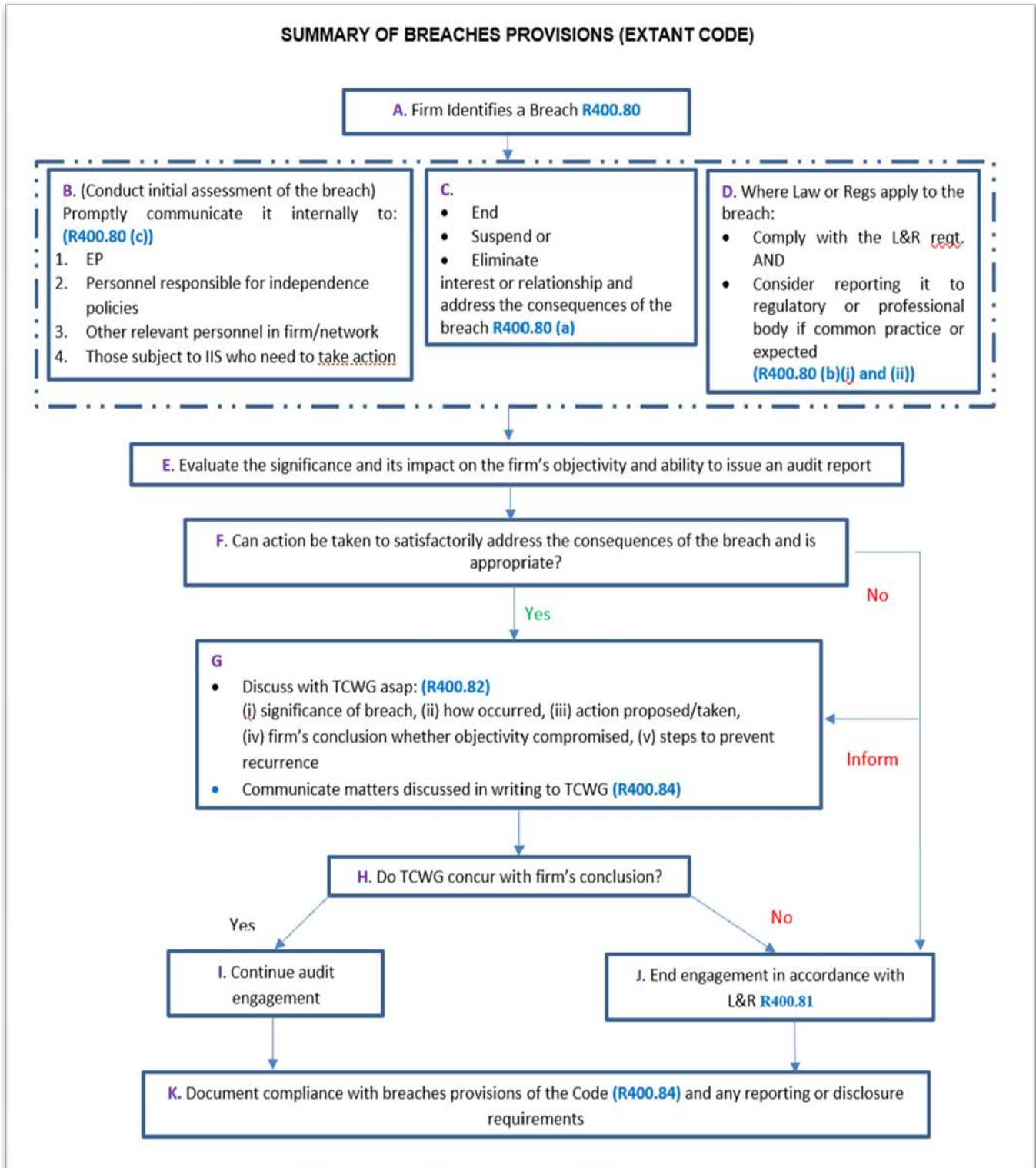
95. In addition to the request for specific comments above, the IESBA is also seeking comments on the matters set out below:

- *Small- and Medium-sized Entities (SMEs) and SMPs* – The IESBA invites comments regarding any aspect of the proposals from SMEs and SMPs.

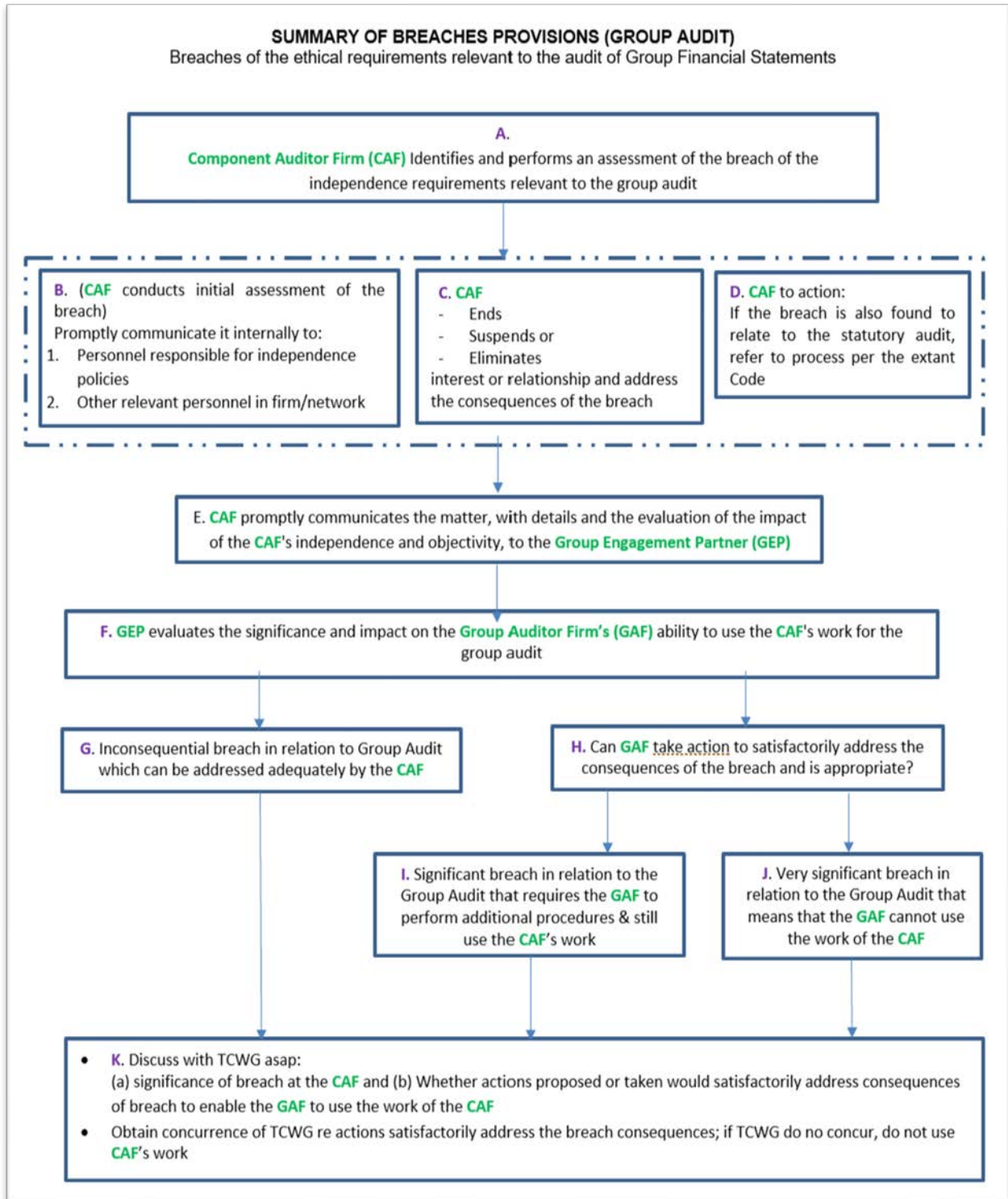
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- *Regulators and Audit Oversight Bodies* – The IESBA invites comments on the proposals from an audit inspection or enforcement perspective from members of the regulatory and audit oversight communities.
- *Developing Nations* – Recognizing that many developing nations have adopted or are in the process of adopting the Code, the IESBA invites respondents from these nations to comment on the proposals, and in particular on any foreseeable difficulties in applying them in their environment.
- *Translations* – Recognizing that many respondents may intend to translate the final changes for adoption in their own environments, the IESBA welcomes comment on potential translation issues respondents may note in reviewing the proposals.

Extant Code Process to Address a Breach of Independence



**Proposed Process to Address a Breach of Independence at a CA Firm (Section 405)**



This Exposure Draft includes proposed revisions as well as consequential and conforming amendments to the Code. These proposals are set out in:

- Chapter 1 – Proposed Changes to the International Independence Standards Relating to the Revision to the Definition of Engagement Team and Group Audits
- Chapter 2 – Proposed Conforming Amendments to Section 360 of the Code to Align with ISA 600 (Revised) Terminology
- Chapter 3 – Proposed Conforming Amendment to Revised Non-assurance Services (NAS) Provisions issued in April 2021
- Chapter 4 – Proposed Conforming Amendments to the Code Resulting from the Revision to the Definition of Engagement Team
- Chapter 5 – Proposed Quality Management-related Consequential Amendments to the Code
- Chapter 6 – Proposed Changes to the Glossary

## **Chapter 1 – Proposed Changes to the International Independence Standards Relating to the Revision to the Definition of Engagement Team and Group Audits**

### **(Mark-up from Extant Code)**

## **PART 4A – INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS**

### **SECTION 400**

### **APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS**

#### **Introduction**

...

400.1 It is in the public interest and required by the Code that professional accountants in public practice be independent when performing audit or review engagements.

400.2 This Part applies to both audit and review engagements. The terms “audit,” “audit team,” “audit engagement,” “audit client,” and “audit report” apply equally to review, review team, review engagement, review client, and review engagement report.

400.3 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.

...

*Note: Paragraph numbers 400.A – 400.D below are placeholders and will be renumbered once the provisions have been finalized and included in Section 400. All paragraphs in Section 400 that follow these new provisions will be renumbered accordingly.*

**Engagement Team and Audit Team**

400.A An engagement team 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.

400.B In ISQM 1, a service provider includes an individual or organization external to the firm that provides a resource that is used in the performance of engagements. Service providers exclude the firm, a network firm or other structures or organizations in the network.

400.C An audit engagement might involve experts from the firm or a network firm, external experts or, in the case of a group audit, experts from a component auditor firm outside the group auditor firm's network, who assist in the engagement. Depending on the role of the individuals, they might be engagement team or audit team members. For example:

- Individuals with expertise in a specialized area of accounting or auditing who perform audit procedures are engagement team members. These include, for example, individuals with expertise in accounting for income taxes or in auditing client information using automated tools and techniques.
- Individuals within or engaged by the 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.
- Individuals who are external experts in fields other than accounting or auditing are neither engagement team nor audit team members.

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.

## **SECTION 405**

### **GROUP AUDITS**

#### **Introduction**

405.1 Section 400 requires a firm to be independent when performing an audit engagement, including a group audit engagement, and to apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence. This section sets out specific requirements and application material relevant to applying the conceptual framework when performing group audit engagements.

#### **Requirements and Application Material**

##### **General**

405.2 A1 The ISAs apply to an audit of group financial statements. This section addresses the relevant independence considerations that apply in a group audit. ISA 600 (Revised) deals with special considerations that apply to an audit of group financial statements, including when component auditors are involved. ISA 600 (Revised) requires the group engagement partner to take responsibility for confirming whether the component auditors understand and will comply with the relevant ethical requirements, including those related to independence, that apply to the group audit. The independence requirements referred to in ISA 600 (Revised), or other relevant auditing standards applicable to group audits that are equivalent to ISA 600 (Revised), are those specified in this section.

405.2 A2 A component auditor firm that participates in a group audit engagement might separately issue an audit opinion on the financial statements of the component audit client. Depending on the circumstances, the component auditor firm might need to comply with different independence requirements when performing audit work for a group audit and separately issuing an audit opinion on the financial statements of the component audit client for statutory, regulatory or other reasons.

##### **Independence Considerations Applicable to Individuals**

R405.3 All members of the audit team for the group audit shall be independent of the group audit client in accordance with the requirements of this Part that are applicable to the audit team.

##### **Independence Considerations Applicable to a Group Auditor Firm**

R405.4 A group auditor firm shall be independent of the group audit client in accordance with the requirements of this Part that are applicable to the firm.

##### **Independence Considerations Applicable to Network Firms of a Group Auditor Firm**

R405.5 A network firm of the group auditor firm shall be independent of the group audit client in accordance with the requirements of this Part that are applicable to the network firm.

**Independence Considerations Applicable to Component Auditor Firms outside a Group Auditor Firm's Network**

*All Group Audit Clients*

**R405.6** A component auditor firm outside the group auditor firm's network:

- (a)** Shall be independent of the component audit client in accordance with the requirements set out in this Part that are applicable to a firm with respect to all audit clients;
- (b)** Shall not hold a direct or material indirect financial interest in the entity on whose group financial statements the group auditor firm expresses an opinion; and
- (c)** Shall, in relation to Section 511 regarding loans and guarantees, apply the relevant specific requirements and application material with respect to the entity on whose group financial statements the group auditor firm expresses an opinion.

**R405.7** When a component auditor firm outside the group auditor firm's network knows, or has reason to believe, that a 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, the component auditor firm shall include that relationship or circumstance when identifying, evaluating and addressing threats to independence.

**R405.8** When a component auditor firm outside the group auditor firm's network knows, or has reason to believe, that a relationship or circumstance of a firm within the component auditor firm's network with the component audit client or the group audit client creates a threat to the component auditor firm's independence, the component auditor firm shall evaluate and address any such threat.

*Group Audit Clients that are Not Public Interest Entities*

**R405.9** When the group audit client is not a public interest entity, a component auditor firm outside the group auditor firm's network shall be independent of the component audit client in accordance with the requirements set out in this Part that are applicable to audit clients that are not public interest entities.

*Group Audit Clients that are Public Interest Entities*

**R405.10** When the group audit client is a public interest entity, a component auditor firm outside the group auditor firm's network shall be independent of the component audit client in accordance with the requirements set out in this Part that are applicable to audit clients that are public interest entities.

**Key Audit Partner**

**405.11 A1** The group engagement partner might determine that an engagement partner who performs audit work related to a component for purposes of the group audit is a key audit partner for the group audit because that individual makes key decisions or judgments on significant matters with respect to the audit of the group financial statements on which the group auditor firm expresses an opinion. In these circumstances, once the group engagement partner has communicated that determination to the engagement partner on the audit of the component, that individual will be subject to the provisions in paragraphs R411.4 and R524.6 and Section



540 that apply to key audit partners.

### Non-Assurance Services

405.12 A1 Section 600 requires a firm to evaluate whether non-assurance services provided to an audit client create threats to independence. The application of paragraph R405.10 requires a component auditor firm to apply the independence requirements for non-assurance services for public interest entities to the component audit client where the group audit client is a public interest entity. For example, where the group audit client is a public interest entity, the component auditor firm is prohibited from acting in an advocacy role for a component audit client that is not a public interest entity in resolving a dispute or litigation before a tribunal or court, regardless of whether the amounts involved are material to the financial information of the component audit client. Similarly, the component auditor firm's design and implementation of the component audit client's information technology system that generates the financial information on which the component auditor firm will perform audit work creates a self-review threat and is therefore prohibited if the group audit client is a public interest entity.

405.12 A2 The financial information on which a component auditor firm performs audit work is relevant to the evaluation of the self-review threat that might be created by the component auditor firm's provision of a non-assurance service. For example, if the component auditor firm's audit work is limited to a specific item such as inventory, the evaluation of the self-review threat would include non-assurance services that form part of or affect the accounting records or the financial information related to the accounting for, or the internal controls over, inventory.

### **Changes in Component Auditor Firms**

#### All Group Audit Clients

405.13 A1 There might be circumstances in which the group auditor firm requests another firm to perform audit work as a component auditor firm during or after the period covered by the group financial statements. A threat to the component auditor firm's independence might be created by:

- (a) Financial or business relationships of the component auditor firm with the component audit client during or after the period covered by the group financial statements but before the component auditor firm agrees to perform the audit work; or
- (b) Previous services provided to the component audit client by the component auditor firm.

405.13 A2 Paragraphs 400.31 A1-A3<sup>37</sup> set out application material that is also applicable for a component auditor firm's assessment of threats to independence if a non-assurance service was provided by the component auditor firm to the component audit client during or after the period covered by the group financial statements, but before the component auditor firm begins to perform the audit work for the purposes of the group audit, and the service would not be permitted during the engagement period.

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<sup>37</sup> The numbering for paragraphs 400.31 A1-A3 will be updated when the revised NAS provisions become effective.

**Breach of an Independence Provision by a Component Auditor Firm**

*When a Component Auditor Firm Within the Group Auditor Firm's Network Identifies a Breach*

**R405.14** If a component auditor firm within the group auditor firm's network concludes that a breach of this section has occurred, the component auditor firm shall communicate the breach immediately to the group engagement partner. Based on the assessment of the component auditor firm's breach, the group engagement partner shall determine what action to take in accordance with the provisions of paragraphs R400.80 to R400.89.

*When a Component Auditor Firm Outside the Group Auditor Firm's Network Identifies a Breach*

**R405.15** If a component auditor firm outside the group auditor firm's network concludes that a breach of this section has occurred, the component auditor firm shall:

- (a)** End, suspend or eliminate the interest or relationship that created the breach and address the consequences of the breach;
- (b)** Evaluate the significance of the breach and its impact on the component auditor firm's objectivity and ability to perform audit work for the purposes of the group audit; (Ref: Para 400.80 A2)
- (c)** Depending on the significance of the breach, determine whether it is possible to take action that satisfactorily addresses the consequences of the breach and whether such action can be taken and is appropriate in the circumstances; and (Ref: Para 400.80 A3)
- (d)** Promptly communicate the breach to the group engagement partner, including the component auditor firm's assessment of the significance of the breach and any actions proposed or taken to address the consequences of the breach.

**R405.16** Upon receipt of the component auditor firm's communication of the breach, the group engagement partner shall:

- (a)** Review the component auditor firm's assessment of the significance of the breach and any actions proposed or taken to address the consequences of the breach;
- (b)** Evaluate the impact of the breach on the component auditor firm's objectivity and the group auditor firm's ability to use the work of the component auditor firm for purposes of the group audit; and
- (c)** Determine the need for any further action.

**R405.17** In making this determination, the group engagement partner shall exercise professional judgment and take into account whether a reasonable and informed third party would be likely to conclude that the component auditor firm's objectivity is compromised, and therefore, the group auditor firm is unable to use the work of the component auditor firm for the purposes of the group audit.

**405.18 A1** If the group engagement partner determines that the breach has been satisfactorily addressed by the component auditor firm and does not compromise the component auditor firm's objectivity, the group auditor firm may continue to use the work of the component auditor firm for the group audit. In certain circumstances, the group engagement partner might determine that additional actions are needed to satisfactorily address the breach in order to use the component auditor firm's work. Examples of such action include the group

auditor firm performing specific procedures on the areas impacted by the breach or requesting the component auditor firm to perform appropriate remedial work on the affected areas.

405.18 A2 If the breach cannot be satisfactorily addressed, the group auditor firm cannot use the component auditor firm's work. In those circumstances, the group engagement partner might find other means to obtain the necessary audit evidence on the component audit client's financial information. Examples of such means include the group auditor firm performing the necessary audit work on the component audit client's financial information or requesting another component auditor firm to perform such audit work.

*Communication with Those Charged with Governance of the Group Audit Client*

**R405.19** With respect to breaches by a component auditor firm outside the group auditor firm's network, the group auditor firm shall discuss with those charged with governance:

- (a)** The significance of the breach at the component auditor firm, including its nature and duration; and
- (b)** Whether actions proposed or taken would satisfactorily address the consequences of the breach to enable the group auditor firm to use the work of the component auditor firm.

Such discussion shall take place as soon as possible unless an alternative timing is specified by those charged with governance for reporting less significant breaches.

**R405.20** If those charged with governance do not concur that the actions proposed or taken satisfactorily address the consequences of the breach at the component auditor firm, the group auditor firm shall not use the work performed by the component auditor firm for the purposes of the group audit.

## Chapter 2 – Proposed Conforming Amendments to Section 360 of the Code to Align with ISA 600 (Revised) Terminology

### (Mark-up from Extant Code)

## PART 3 - PROFESSIONAL ACCOUNTANTS IN PUBLIC PRACTICE

### SECTION 360

### RESPONDING TO NON-COMPLIANCE WITH LAWS AND REGULATIONS

#### Communication with Respect to Groups

**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 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 ~~the a~~ component for 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.

The communication to the group engagement partner shall be in addition to responding to the matter in accordance with the provisions of this section.

360.16 A1 The purpose of the communication is to enable the group engagement partner to be informed about the matter and to determine, in the context of the group audit, whether and, if so, how to address it in accordance with the provisions in this section. The communication requirement in paragraph R360.16 applies regardless of whether the group engagement partner's firm or network is the same as or different from the professional accountant's firm or network.

**R360.17** Where the group engagement partner becomes aware of non-compliance or suspected non-compliance in the course of ~~a group audit of group financial statements~~, the group engagement partner shall consider whether the matter might be relevant to ~~one or more components~~:

- (a) One or more components ~~Whose financial information is~~ subject to audit work for purposes of the ~~audit of the group~~ audit financial statements; or
- (b) One or more legal entities or business units that are part of the group and ~~Whose~~ financial statements are subject to audit for purposes other than the group audit, for example, a statutory audit.

This consideration shall be in addition to responding to the matter in the context of the group audit in accordance with the provisions of this section.

**R360.18** If the non-compliance or suspected non-compliance might be relevant to one or more of the components, legal entities or business units specified in paragraph R360.17(a) and (b), the

group engagement partner shall take steps to have the matter communicated to those performing audit work at the components, legal entities or business units, unless prohibited from doing so by law or regulation. If necessary, the group engagement partner shall arrange for appropriate inquiries to be made (either of management or from publicly available information) as to whether the relevant ~~component(s)~~ legal entities or business units specified in paragraph R360.17 (b) are subject to audit and, if so, to ascertain to the extent practicable the identity of the auditors.

360.18 A1 The purpose of the communication is to enable those responsible for audit work at the components, legal entities or business units to be informed about the matter and to determine whether and, if so, how to address it in accordance with the provisions in this section. The communication requirement applies regardless of whether the group engagement partner's firm or network is the same as or different from the firms or networks of those performing audit work at the components, legal entities or business units.

**Chapter 3 – Proposed Conforming Amendment to Revised Non-assurance Services (NAS) Provisions issued in April 2021**

**(Mark-up from Revised NAS Provisions)**

**PART 4A – INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS**

**SECTION 400**

**APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS**

**Requirements and Application Material**

...

**R400.31** If an entity becomes an audit client during or after the period covered by the financial statements on which the firm will express an opinion, the firm shall determine whether any threats to independence are created by:

- (a) Financial or business relationships with the audit client during or after the period covered by the financial statements but before accepting the audit engagement; or
- (b) Previous Sservices provided to the audit client by the firm or a network firm ~~in prior financial statement periods.~~

**Chapter 4 – Proposed Conforming Amendments to the Code Resulting from the Revision to the Definition of Engagement Team**

**(Mark-up from Extant Code)**

**PART 3 - PROFESSIONAL ACCOUNTANTS IN PUBLIC PRACTICE**

**SECTION 300**

**APPLYING THE CONCEPTUAL FRAMEWORK – PROFESSIONAL ACCOUNTANTS IN PUBLIC PRACTICE**

**Requirements and Application Material**

**General**

...

**Addressing Threats**

...

*Examples of Safeguards*

300.8 A2 Safeguards vary depending on the facts and circumstances. Examples of actions that in certain circumstances might be safeguards to address threats include:

- ...
- Using different partners and ~~engagement~~ teams with separate reporting lines for the provision of non-assurance services to an assurance client might address self-review, advocacy or familiarity threats.
- ...

## SECTION 310 CONFLICTS OF INTEREST

### Conflict Identification

...

### Threats Created by Conflicts of Interest

...

310.8 A3 Examples of actions that might be safeguards to address threats created by a conflict of interest include:

- Having separate ~~engagement~~ teams who are provided with clear policies and procedures on maintaining confidentiality.
- ...

### Confidentiality

...

#### *When Disclosure to Obtain Consent would Breach Confidentiality*

**R310.12** When making specific disclosure for the purpose of obtaining explicit consent would result in a breach of confidentiality, and such consent cannot therefore be obtained, the firm shall only accept or continue an engagement if:

- (a) The firm does not act in an advocacy role for one client in an adversarial position against another client in the same matter;
- (b) Specific measures are in place to prevent disclosure of confidential information between the ~~engagement~~ teams serving the two clients; and

...

### Documentation

**R310.13** In the circumstances set out in paragraph R310.12, the professional accountant shall document:

- (a) The nature of the circumstances, including the role that the accountant is to undertake;
- (b) The specific measures in place to prevent disclosure of information between the ~~engagement~~ teams serving the two clients; and

...



**SECTION 320**  
**PROFESSIONAL APPOINTMENTS**

...

**Requirements and Application Material**

**Client and Engagement Acceptance**

*General*

320.3 A3 A self-interest threat to compliance with the principle of professional competence and due care is created if the ~~engagement~~-team does not possess, or cannot acquire, the competencies to perform the professional services.

...

## INTERNATIONAL INDEPENDENCE STANDARDS

### PART 4A – INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS

#### SECTION 400

#### APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS

...

#### Requirements and Application Material

...

#### Period During which Independence is Required

...

400.30 A1 The engagement period starts when the audit engagement team begins to perform the audit. The engagement period ends when the audit report is issued. When the engagement is of a recurring nature, it ends at the later of the notification by either party that the professional relationship has ended or the issuance of the final audit report.

...

400.31 A1 Threats to independence are created if a non-assurance service was provided to an audit client during, or after the period covered by the financial statements, but before the audit engagement team begins to perform the audit, and the service would not be permitted during the engagement period.

#### SECTION 510

#### FINANCIAL INTERESTS

#### Requirements and Application Material

...

#### Financial Interests Held by the Firm, a Network Firm, Audit Team Members and Others

...

510.4 A1 The office in which the engagement partner practices in connection with an audit engagement is not necessarily the office to which that partner is assigned. When the engagement partner is located in a different office from that of the other audit engagement team members, professional judgment is needed to determine the office in which the partner practices in connection with the engagement.

...

## SUBSECTION 605 – INTERNAL AUDIT SERVICES (FROM REVISED NAS PRONOUNCEMENT)

### Introduction

...

### Requirements and Application Material

...

605.4 A2 When a firm uses the work of an internal audit function in an audit engagement, ISAs require the performance of procedures to evaluate the adequacy of that work. Similarly, when a firm or network firm accepts an engagement to provide internal audit services to an audit client, the results of those services might be used in conducting the external audit. This might create a self-review threat because it is possible that the ~~audit engagement~~ team will use the results of the internal audit service for purposes of the audit engagement without:

- (a) Appropriately evaluating those results; or
- (b) Exercising the same level of professional skepticism as would be exercised when the internal audit work is performed by individuals who are not members of the firm.

605.4 A3 Factors that are relevant in identifying a self-review threat created by providing internal audit services to an audit client, and evaluating the level of such threat include:

- The materiality of the related financial statement amounts.
- The risk of misstatement of the assertions related to those financial statement amounts.
- The degree of reliance that the ~~audit engagement~~ team will place on the work of the internal audit service.

When a self-review threat for an audit client that is a public interest entity has been identified, paragraph R605.6 applies.

**PART 4B (REVISED) – INDEPENDENCE FOR ASSURANCE ENGAGEMENTS  
OTHER THAN AUDIT AND REVIEW ENGAGEMENTS**

**SECTION 900**

**APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR  
ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW  
ENGAGEMENTS**

...

**Requirements and Application Material**

...

**Period During which Independence is Required**

**R900.30** Independence, as required by this Part, shall be maintained during both:

- (a) The engagement period; and
- (b) The period covered by the subject matter information.

900.30 A1 The engagement period starts when the ~~assurance engagement~~ team begins to perform assurance services with respect to the particular engagement. The engagement period ends when the assurance report is issued. When the engagement is of a recurring nature, it ends at the later of the notification by either party that the professional relationship has ended or the issuance of the final assurance report.

...

**R900.32** Threats to independence are created if a non-assurance service was provided to the assurance client during, or after the period covered by the subject matter information, but before the ~~assurance engagement~~ team begins to perform assurance services, and the service would not be permitted during the engagement period. In such circumstances, the firm shall evaluate and address any threat to independence created by the service. If the threats are not at an acceptable level, the firm shall only accept the assurance engagement if the threats are reduced to an acceptable level.

## Chapter 5 – Proposed Quality Management-related Consequential Amendments to the Code

### INTERNATIONAL INDEPENDENCE STANDARDS

#### (MARK-UP FROM EXTANT CODE)

#### PART 4A – INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS

##### SECTION 540

##### LONG ASSOCIATION OF PERSONNEL (INCLUDING PARTNER ROTATION) WITH AN AUDIT CLIENT

##### Requirements and Application Material

###### All Audit Clients

...

**R540.4** If a firm decides that the level of the threats created can only be addressed by rotating the individual off the audit team, the firm shall determine an appropriate period during which the individual shall not:

- (a) Be a member of the engagement team for the audit engagement;
- (b) ~~Provide quality control for the audit engagement~~Perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the engagement; or
- (c) Exert direct influence on the outcome of the audit engagement.

The period shall be of sufficient duration to allow the familiarity and self-interest threats to be addressed. In the case of a public interest entity, paragraphs R540.5 to R540.20 also apply.

...

###### Restrictions on Activities During the Cooling-off Period

**R540.20** For the duration of the relevant cooling-off period, the individual shall not:

- (a) Be an engagement team member or ~~provide quality control~~perform an engagement quality review, or a review consistent with the objective of an engagement quality review for the audit engagement;
- (b) Consult with the engagement team or the client regarding technical or industry-specific issues, transactions or events affecting the audit engagement (other than discussions with the engagement team limited to work undertaken or conclusions reached in the last year of the individual's time-on period where this remains relevant to the audit);
- (c) Be responsible for leading or coordinating the professional services provided by the firm or a network firm to the audit client, or overseeing the relationship of the firm or a network firm with the audit client; or
- (d) Undertake any other role or activity not referred to above with respect to the audit client, including the provision of non-assurance services that would result in the individual:

- (i) Having significant or frequent interaction with senior management or those charged with governance; or
- (ii) Exerting direct influence on the outcome of the audit engagement.

...

## SECTION 800

### REPORTS ON SPECIAL PURPOSE FINANCIAL STATEMENTS THAT INCLUDE A RESTRICTION ON USE AND DISTRIBUTION (AUDIT AND REVIEW ENGAGEMENTS)

#### Requirements and Application Material

##### General

##### Financial Interests, Loans and Guarantees, Close Business Relationships, and Family and Personal Relationships

**R800.10** When the firm performs an eligible audit engagement:

- (a) The relevant provisions set out in Sections 510, 511, 520, 521, 522, 524 and 525 need apply only to the members of the engagement team, their immediate family members and, where applicable, close family members;
- (b) The firm shall identify, evaluate and address any threats to independence created by interests and relationships, as set out in Sections 510, 511, 520, 521, 522, 524 and 525, between the audit client and the following audit team members:
  - (i) Those who provide consultation regarding technical or industry specific issues, transactions or events; and
  - (ii) ~~Those who provide quality control for the engagement, including those who perform the engagement quality control review~~ Those who perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the engagement; and
- (c) The firm shall evaluate and address any threats that the engagement team has reason to believe are created by interests and relationships between the audit client and others within the firm who can directly influence the outcome of the audit engagement.

## PART 4B (REVISED) – INDEPENDENCE FOR ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS

### SECTION 940

#### LONG ASSOCIATION OF PERSONNEL WITH AN ASSURANCE CLIENT

##### Requirements and Application Material

###### General

...

**R940.4** If a firm decides that the level of the threats created can only be addressed by rotating the individual off the assurance team, the firm shall determine an appropriate period during which the individual shall not:

- (a) Be a member of the engagement team for the assurance engagement;
- (b) ~~Provide quality control for the assurance engagement~~Perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the engagement; or
- (c) Exert direct influence on the outcome of the assurance engagement.

The period shall be of sufficient duration to allow the familiarity and self-interest threats to be addressed.

### SECTION 990

#### REPORTS THAT INCLUDE A RESTRICTION ON USE AND DISTRIBUTION (ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS)

##### Financial Interests, Loans and Guarantees, Close Business, Family and Personal Relationships

**R990.7** When the firm performs an eligible assurance engagement:

- (a) The relevant provisions set out in Sections 910, 911, 920, 921, 922 and 924 need apply only to the members of the engagement team, and their immediate and close family members;
- (b) The firm shall identify, evaluate and address any threats to independence created by interests and relationships, as set out in Sections 910, 911, 920, 921, 922 and 924, between the assurance client and the following assurance team members:
  - (i) Those who provide consultation regarding technical or industry specific issues, transactions or events; and
  - (ii) ~~Those who provide quality control for the engagement, including those who perform the engagement quality control review~~Those who perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the engagement; and
- (c) The firm shall evaluate and address any threats that the engagement team has reason to believe are created by interests and relationships between the assurance client and others within the firm who can directly influence the outcome of the assurance engagement, as set out in Sections 910, 911, 920, 921, 922 and 924.

## Chapter 6: Proposed Changes to the Glossary

### (Mark-up from Extant Code)

- Assurance Team
- (a) All members of the engagement team for the assurance engagement;
  - (b) All others within, or engaged by, a-the firm who can directly influence the outcome of the assurance engagement, including:
    - (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the assurance engagement partner in connection with the performance of the assurance engagement;
    - (ii) Those who provide consultation regarding technical or industry specific issues, transactions or events for the assurance engagement; and
    - (iii) Those who ~~provide~~ perform an engagement quality control review, or a review consistent with the objective of an engagement quality review, for the ~~assurance engagement, including those who perform the engagement quality control review for the assurance engagement.~~

- Audit Team
- (a) All members of the engagement team for the audit engagement;
  - (b) All others within, or engaged by, a-the firm who can directly influence the outcome of the audit engagement, including:
    - (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the engagement partner in connection with the performance of the audit engagement, including those at all successively senior levels above the engagement partner through to the individual who is the firm's Senior or Managing Partner (Chief Executive or equivalent);
    - (ii) Those who provide consultation regarding technical or industry-specific issues, transactions or events for the engagement; and
    - (iii) Those who ~~provide~~ perform an engagement quality control for the engagement, including those who perform the review, or a review consistent with the objective of an engagement quality ~~control~~ review, for the engagement; and
  - (c) All those within a network firm who can directly influence the outcome of the audit engagement.

*In Part 4A, the term "audit team" applies equally to "review team."*

- 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;
  - (b) All others within, or engaged by, the group auditor firm who can directly



influence the outcome of the group audit, including:

- (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the group engagement partner in connection with the performance of the group audit, including those at all successively senior levels above the group engagement partner through to the individual who is the firm’s Senior or Managing Partner (Chief Executive or equivalent);
- (ii) Those who provide consultation regarding technical or industry-specific issues, transactions or events for the group audit; and
- (iii) Those who perform an engagement quality review, or a review consistent with the objective of an engagement quality review, for the group audit;
- (c) All those within a network firm of the group auditor firm’s network who can directly influence the outcome of the group audit; and
- (d) Any individual within a component auditor firm outside the group auditor firm’s network who can directly influence the outcome of the group audit.

Component 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

Component audit client When a component is:

- (a) A legal entity, the entity and any related entities over which the entity has direct or indirect control; or
- (b) A business unit, function or business activity (or some combination thereof), the legal entity or entities to which the business unit belongs or in which the function or business activity is being performed.

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

Engagement team All partners and staff performing the engagement, and any ~~other~~ individuals ~~engaged by the firm or a network firm~~ who perform ~~assurance~~ procedures on the engagement, ~~excluding external experts and internal auditors who provide direct assistance on the engagement. This excludes external experts engaged by the firm or by a network firm.~~

~~The term “engagement team” also excludes individuals within the client’s internal audit function who provide direct assistance on an audit engagement when the external auditor complies with the requirements of ISA 610 (Revised 2013), *Using the Work of Internal Auditors*.~~

*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.

ISA 220 (Revised) provides further guidance on the definition of engagement team in the context of an audit of financial statements.

ISA 620 deals with the auditor’s responsibilities relating to the work of an individual or organization in a field of expertise other than accounting or auditing, when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence.

ISA 610 (Revised 2013) deals with the auditor’s responsibilities if using the work of internal auditors, including using internal auditors to provide direct assistance on the audit engagement.

In Part 4B, the term “engagement team” refers to individuals performing assurance procedures on the assurance engagement.

<u>Group</u>	<u>A reporting entity for which group financial statements are prepared</u>
<u>Group audit</u>	<u>The audit of group financial statements</u>
<u>Group audit client</u>	<u>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.</u>
<u>Group auditor firm</u>	<u>The firm that expresses the opinion on the group financial statements</u>
<u>Group engagement partner</u>	<u>The engagement partner who is responsible for the group audit</u>
<u>Group financial statements</u>	<u>Financial statements that include the financial information of more than one entity or business unit through a consolidation process</u>
Key audit partner	The engagement partner, the individual responsible for the engagement quality review, and other audit partners, if any, on the engagement team who make key decisions or judgments on significant matters with respect to the audit of the financial statements on which the firm will express an opinion. Depending upon the circumstances and the role of the individuals on the audit, “other audit partners” might include, for example, <u>audit engagement partners responsible for certain components in a group audit such as</u> significant subsidiaries or divisions.
Review team	(a) All members of the engagement team for the review engagement; and (b) All others within, <u>or engaged by, a—the</u> firm who can directly influence the outcome of the review engagement, including:

- (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the engagement partner in connection with the performance of the review engagement, including those at all successively senior levels above the engagement partner through to the individual who is the firm's Senior or Managing Partner (Chief Executive or equivalent);
  - (ii) Those who provide consultation regarding technical or industry specific issues, transactions or events for the engagement; and
  - (iii) Those who ~~provide~~ perform an engagement quality review, or a review consistent with the objective of an engagement quality review, quality control for the engagement, ~~including those who perform the engagement quality control review for the engagement~~; and
- (c) All those within a network firm who can directly influence the outcome of the review engagement.

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