Compilation of Comments to ET/GA ED – Question 8

Note to IESBA Meeting Participants
This reference document includes the compilation of the comments from the 49 comment letters submitted in response to the following Question 8 of Exposure Draft, Proposed Revisions to the Code Relating to the Definition of Engagement Team and Group Audits (ED):

“Breach of Independence by a Component Auditor Firm

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

For the analysis of all significant comments and the Task Force’s responses, please refer to Agenda Items 5-A and 5-B.

Regulators and Oversight Authorities, Including MG members

1. The Botswana Accountancy Oversight Authority (BAOA)

Yes, we agree. The proposed remedial actions to be considered and undertaken by the Component Auditor are considered appropriate. The proposal to give the group auditor the responsibility to conclude on the threat to independence is also appropriate to ensure that another auditor who is not directly affected by the threat reviews circumstances surrounding the threat to independence. This would help to ultimately take a decision of whether reliance can be placed on the CA’s work.

2. Committee of European Auditing Oversight Bodies (CEAOB)

Breach of independence by component auditor firm

(Revised) ISA 600 states in paragraph 25 the responsibilities of the group engagement partner regarding the component auditors’ compliance with relevant ethical requirements. We believe that the component auditor firm outside of the group auditor firm’s network should be required to inform the group auditor when it applies the "reason to believe" tests referred to in paragraphs R405.7 and R405.8 whether or not these lead to a threat to independence.

Paragraph 405.18 A1 states that additional actions might be needed to satisfactorily address breaches of independence by the component auditor firm. We support this remedial work, however we suggest emphasizing in paragraph 405.18 A1 that the group auditor firm should assess the remedial actions identified as necessary by the group engagement partner, whether performed by the group auditor firm or by the component auditor. In addition, we suggest clarifying the rationale when it would be appropriate that the component auditor firm where the independence breach was identified also performs remedial work in relation to the affected areas

Communication with those charged with governance of the group audit client

With respect to paragraphs R405.19 and R405.20 on communicating to those charged with governance (“TCWG”) of the group audit client, we suggest that all breaches by component auditors, regardless of whether they are part of the group auditor firm’s network, require the same information and discussion/decision making at TCWG level. If this is already required elsewhere in the Code, it would be useful to include references to the requirements regarding communications with TCWG relating to breaches by component audit firms within the group auditor’s network.

We also suggest clarifying whether the requirement in paragraph R400.84 about communicating in writing about breaches to those charged with governance only applies to the group audit firm.

Finally, we suggest repeating in paragraphs R405.19 and R405.20 that these communications take place with those charged with governance of the group audit client (in addition to the header).
3. International Forum of Independent Audit Regulators (IFIAR)

**Breach of independence by a Component Auditor Firm**

R405.14 of the Code, related to breaches of independence when a component auditor firm within the group auditor firm’s network concludes that a breach has occurred, is less restrictive than R405.15 of the Code, related to breaches of independence when a component auditor outside the group auditor’s firm network concludes that a breach has occurred, because R405.14 would allow a decision by the group engagement partner to determine what action to take in accordance with the provisions of paragraphs R400.80 to R400.89. Comparatively, R405.15, would state, among other things, that the interest or relationship causing the breach must be ended, suspended, or eliminated. We think that a differentiation in the consequences between component firms within and outside of the network is neither appropriate nor aligns with the network neutrality as envisaged by ISA 600 (Revised).

It is not clear enough why the requirement in R405.19 of the Code for the group auditor firm to communicate breaches by a component auditor firm outside the group auditor firm’s network to those charged with governance of the group audit client is not the same as the provisions applicable for other breaches in extant paragraph R400.84 of the Code (i.e., discussion, as per R405.19, versus written communications as per extant paragraph R400.84). We suggest that all breaches, regardless of the component auditor that commits them, require the same method of communication to those charged with governance of the group audit client.

Additionally, we believe it would be beneficial to specify in the body of paragraphs R405.19 and R405.20 of the Code that communication should be with those charged with governance of the group audit client (instead of this specification appearing only in the header to those paragraphs).

4. International Organization of Securities Commissions (IOSCO)

**Observations**

**Section 405. Group Audits**

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

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<th>Paragraph</th>
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<td>405.18 A1</td>
<td>This paragraph acknowledges that following the occurrence of a breach within a CA firm outside the group auditor’s firm network, in certain circumstances, the group engagement partner might determine that in order to use the CA firm’s work, additional actions are needed to satisfactorily address the breach, including, for example, requesting the same CA firm to perform appropriate remedial work on the affected areas. We observe that allowing for the CA firm to perform remedial work on areas of the engagement that are affected by its own breach may not be an appropriate safeguard. For example, if the CA firm (or a firm in its network) provides a service that results in a breach due to a self-review threat, we question the notion of the same CA firm performing remedial work. Further, in this scenario, the CA firm may be incentivized to make judgments that prioritize the economics and other interests of the CA firm over the public interest, including investors. To avoid these types of self-interest conflicts, examples of other safeguards that could be taken, include the following:</td>
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<td>• Recommend that the component audit client engage another firm to review or re-perform the affected audit work, to the extent necessary.</td>
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• The group auditor should evaluate, or re-perform the affected audit work, or engage another firm to evaluate the results of the non-assurance service or re-perform the non-assurance service, to the extent necessary. Further, we believe that it would be useful for the Board to provide examples of the circumstances in which the group engagement partner may determine that additional actions are required or are not required. We believe this would be helpful for the group engagement partner in exercising his or her judgment. Moreover, for those situations in which the Board believes such additional actions must be taken, there should be guidance on how and what the group engagement partner could consider in performing appropriate remedial work to address the breach.

5. Independent Regulatory Board for Auditors (South Africa) (IRBA)

The IRBA recommends that the requirements in Section 405 be clarified to state who in the component auditor firm is responsible for the performance of the procedures required in paragraphs R405.7, R405.8 and R405.15.

We further propose that the IESBA considers including a requirement for firms outside of the group auditor firm’s network to inform the group auditor of any relationships and circumstances that are being evaluated for threats (R405.7) – whether these lead to a threat to the component auditor firm’s independence (R405.8). Paragraph R405.8, regarding the threat to the component auditor firm’s independence, leaves the independence threat evaluation to the component auditor firm. We propose that the component auditor firm must communicate all independence threats and the appropriate safeguards taken to the group auditor firm. This will assist with applying the IESBA Code consistently across the group.

Paragraph R405.14 on component auditor firms within the network is less restrictive in the event of breaches (by allowing a decision by the group engagement partner) than paragraph R405.15 on component auditor firms outside of the group auditor firm’s network. In the latter case, the relationship causing the breach must be ended, eliminated or suspended. We think that a differentiation in the consequences between component firms within and outside of the network is not appropriate and does not align with the network neutral character envisaged by ISA 600 (Revised).

In addition, we suggest that paragraphs R405.16 and R405.17, regarding the group engagement partner’s responses to any communication about a breach at a component auditor firm, should also apply to reported breaches by component auditor firms outside of the group auditor firm’s network. Currently, these read as though they only encompass a scenario where a component auditor firm within the group auditor firm’s network identifies a breach.

Lastly, it is unclear why the requirement in paragraph R405.19 to communicate breaches by a component auditor firm outside the group auditor firm’s network to TCWG is different from the provisions applicable for other breaches in paragraph R400.84 (i.e., discussion as per R405.19 versus written communication as per 400.84). Additionally, it would seem helpful to clarify that the communication should be with TCWG of the group audit client. We therefore suggest that all breaches, regardless of the component in which they occur, require similar information and discussion/decision-making at the TCWG level.

6. National Association of State Boards of Accountancy (US) (NASBA)

NASBA believes that the process proposed by IESBA is appropriate when there is a breach of independence by a non-network CA. Notification of the group engagement partner (GEP) by the non-network CA is an essential component of the process. Ultimately, it is the responsibility of the GEP to determine the significance of the breach and what, if any actions may be taken to use the work of the non-network CA. It is also appropriate for the GA firm to notify those charged with governance (TCWG) of the breach at the CA firm and the remedial actions taken by the GA firm, if any. Similarly, NASBA supports IESBA’s proposal to prohibit the GA firm from using the work of the CA firm for purposes of the group audit if TCWG do not concur with the GA firm’s assessment.

7. United Kingdom Financial Reporting Council (UK FRC)
The procedures to address a breach of independence within the Group Auditor’s network are a logical extension of circumstances where a breach has taken place within the Group Auditor firm itself. For situations where the Component Auditor is outside the Group Auditor network, as the guidance notes, the Group Auditor firm cannot monitor or implement procedures to ensure compliance. The proposed revisions to the Code would be improved if clarity was provided on who within the Component Auditor firm is responsible for the performance of the specific procedures set out in paragraphs R405.7, R405.8 and R405.15.

We note that requirements set out in R405.14 for Component Auditor firms inside the Group Auditor’s network is less restrictive for instances of breaches than in R405.15 for Component Auditor firms outside of that network. In the former, the Group Engagement Partner is allowed discretion to conclude whether the breach of independence requirements has been mitigated appropriately, whereas in the latter the relationship causing the breach must be removed. We do not believe this differentiation is appropriate, and that it is contrary to ISA 600 (Revised) which does not differentiate requirements for Component Auditors on whether they are a member of the Group Auditor’s network or otherwise. The IESBA Code should set the same requirements for all Component Auditors, regardless of whether they are within the Group Auditor’s network or not.

Public Sector Organizations

8. United States Government Accountability Office (GAO)

We believe that the proposals in section 405 for addressing a breach of independence by a component auditor firm are appropriate. For paragraph 405.18 A2, we suggest that the guidance be revised to indicate that the group auditor firm determines whether sufficient audit evidence may be obtained.

Independent National Standard Setters

9. Accounting Professional & Ethical Standards Board Australia (APESB)

APESB agrees with the proposals in Section 405 to address the breaches of Independence, and is supportive of the additional proposals to address component audit firms that are outside the group audit firm’s network.

Feedback from stakeholders in Australia also showed support for the proposed revisions to address breaches of independence by a component firm. It was acknowledged that the group engagement partner is responsible for the overall Independence of the group audit engagement. However, when possible, it may be beneficial for the component auditor to be involved in the communication with those charged with governance to discuss any breaches of independence by the component firm.

From an editorial perspective, APESB have noted the following two matters for the IESBA’s consideration:

- proposed paragraph R405.14 must be split into two separate provisions/paragraphs from an enforcement perspective. The proposed drafting has two sentences, with each sentence imposing requirements on two different parties (i.e., the component auditor firm and then the group engagement partner). It would have more impact if the requirement on each party were in a separate provision; and
- proposed paragraph R405.17 should include a cross-reference to proposed paragraph R405.16 rather than stating ‘this determination’. For example, “In making the determination in paragraph R405.16, the ...”

Recommendation

- Consider whether the component auditor should be involved in the communication with those charged with governance of the group audit client if the breach of independence relates to the component audit firm; and
- Consider the simplification of terms and language used in the revised provisions in Section 405 to enhance the ability of readers to easily understand, comprehend and interpret the provisions (refer to issues raised in Questions 1, 3, 4, 6, 7 and 8 in Appendix A)
10. **New Zealand Auditing & Assurance Standard Board (NZAuASB)**

Yes, the NZAuASB supports the proposals and does not have any further comments.

**Professional Accountancy Organizations**

11. **Joint Submission -- Association of Chartered Certified Accountants/Chartered Accountants Australia and New Zealand (ACCA CAANZ)**

Yes, we agree with the proposals in Section 405.

12. **Accountancy Europe (AE)**

13. **American Institute of Certified Public Accountants' Professional Ethics Executive Committee (AICPA PEEC)**

PEEC supports the proposals in Section 405 of the IESBA code to address a breach of independence by a component audit firm whether the component audit firm is within the group audit firm's network or is a non-network component audit firm.

14. **Botswana Institute of Chartered Accountants (BICA)**

Yes, we agree with the proposed requirements and guidance in Section 405 to deal with circumstances where a breach is identified at the CA firm level. The process that a firm should follow when it concludes that a breach of a requirement of the International Independence Standards (IIS) has occurred as set out in Appendix 1 is also sufficiently clear.

15. **Chartered Accountants Ireland (CAI)**

The flowcharts in Appendices 1 and 2 contain helpful guidance. We recommend that they are included in the standard as application guidance.

16. **CPA Australia (CPAA)**

CPA Australia agrees with the proposals in Section 405 to address a breach of independence by a component auditor firm.

17. **Chartered Professional Accountants of Canada Public Trust Committee (CPAC)**

The PTC is supportive of the IESBA’s proposals to outline the process to be followed in the event of a breach of independence. Our stakeholders note that the Appendix 2 in relation to the breach of independence at a CA firm is very useful and recommend it be directly included in the Code, or in a readily accessible guidance document.

We observe that the IESBA has not identified an option to end the audit engagement in the event of a breach in proposed paragraph R405.15. We assume that the IESBA’s intent is that the group engagement partner is the one to consider whether to end the audit engagement, and therefore it is not addressed in this proposed section, however we recommend that the IESBA considers whether this can be clarified in the final revisions.

18. **Compagnie Nationale des Commissaires aux Comptes (CNCC)**

We agree with the principles for the auditor to analyse the impact of breaches of independence and escalate them to those charged with governance to see whether they concur with the auditor's conclusion as to the significance (or not) of the breach. It is globally the same rationale as in the extant code.

In addition, we believe that the group auditor will not be able to identify breaches of independence of non-network component auditors and that in practice s/he will not be able to know whether the non-network component auditor of a non-PIE component has followed the PIE independence rules on the component or not.
19. European Federation of Accountants and Auditors for SMEs (EFAA)
We agree.

20. Federación Argentina de Consejos Profesionales de Ciencias Económicas (FACPCE)
Yes. We agree that the process for addressing a breach of independence is more direct and effective when the component auditor (CA) is a member firm of the group auditor's (GA) network of firms. Some limitations or practical problems may arise when the CA is outside the GA signature network.

We agree that it would not be in the public interest to question the reliability of all the work done in a group audit, if the non-compliance in relation to one component was inadvertent and insignificant. Prompt communication of the situation to the Group Audit Partner (GEP), along with an assessment of the significance of the non-compliance, its potential effects and any actions to address it, are essential.

We agree with the guidelines suggested by the IESBA, and the interaction between Section 405 of the Code of Ethics and ISA 600 (Revised).

One issue that may be explored by the IESBA is the potential reporting - by the AG - of a breach of independence by a CA outside its network, to a regulator or audit supervisor. This regulatory or supervisory body should evaluate the case raised, giving rise to any discharge by the CA and consideration by the TCWG of the audited entity, and eventually take the appropriate disciplinary measures, measures that the GA auditor cannot take because the CA is outside your network. An additional issue to consider is how to deal with these disciplinary issues when the CA is from a different jurisdiction than the AG (for example, from another country with its own regulations).

21. Hong Kong Institute of Certified Public Accountants (HKICPA)
R405.7 and R405.8 specify that if the CA firm becomes aware of a specified relationship or circumstance indicating a potential threat to its independence, it should evaluate its independence against the situation identified and address those threats, if appropriate.

While the CA firm may address such situations appropriately without breaching the independence requirements, we suggest the Code to require the CA firm to inform the GA firm of such circumstances, including the CA firm's assessment and actions taken, for the GA firm to evaluate whether there are other aspects relating to the circumstances that could trigger independence concerns at the group level or among other CA firms.

22. Instituto dos Auditores Independentes do Brasil (Ibracon)
We agree with the proposals in Section 405 to address a breach of independence by a CA firm, including the communication by the GA with Those Charged with Governance of the Group Audit Client.

23. Institute of Chartered Accountants of Scotland (ICAS)
Yes - we agree with the proposals in Section 405 to address a breach of independence by a CA firm.

24. Institute of Chartered Accountants in England and Wales (ICAEW)
We are generally supportive of the proposals though we do not think that it is entirely clear what the practical differences will be with the proposed slightly different treatment between network component auditor firms and non-network component auditor firms (which has led to the separate non-network requirements in R405.15 – 20).

The table in Appendix 2 illustrates the process to address breaches but the distinction between significant and very significant breaches is not entirely clear and might not be necessary. It also does not appear to distinguish between the resulting actions based on whether the component auditor firm is within or outside the Network.

25. Institute of Certified Public Accountants of Uganda (ICPAU)
We agree with the proposals in Section 405 to address a breach of independence by a Component Auditor firm.
26. Institut der Wirtschaftsprüfer (Germany) (IDW)

As explained above, we suggest that an approach that includes de minimis exceptions be considered, as we suspect that the Proposal will lead to irritation and potentially be a further factor in driving changes in the audit market.

27. Institute of Singapore Chartered Accountants (ISCA)

28. Japanese Institute of Certified Public Accountants (JICPA)

We agree with the proposal in Section 405 to address a breach of independence by a component auditor firm, except for the following.

The proposed paragraph R405.19 of the Exposure Draft requires that the group auditor firm to discuss with those charged with governance the significance of the breach at the component auditor firm and whether actions proposed or taken would satisfactorily address the consequence of the breach to enable the group auditor firm to use the work of the component auditor firm. However, the paragraph does not state the discussion where the group auditor may not use the work of the component auditor firm. The paragraph should be consistent with APPENDIX 2 that describes necessity of the discussion with those charged with governance in case the group auditor firm may not use the work of the component auditor firm because the breach at the component auditor firm is "very significant." Specifically, in paragraph R405.19 (a), in addition to the severity of the violation, we propose that the paragraph should state whether the group auditor firm may use the work of the component auditor firm by taking the necessary actions and, if not, what the group auditor firm should do to express its opinion.

29. Korean Institute of Certified Public Accountants (KICPA)

We believe that the proposals are consistent with the general principles of the Code relating to the breach of independence (R400.80). We agree with the proposals as they set forth requirements and application guidance to apply the general principles in the context of group audit.

30. Malaysian Institute of Accountants (MIA)

We agree with the proposals contained in paragraph R405.14 relating to a breach identified by a component auditor firm with the group auditor firm’s network.

With respect to the proposals relating to a breach identified by a component auditor firm outside the group auditor firm’s network, we are of the view that a necessary step for the component auditor firm is missing, namely, to consider whether, and appropriately respond to any legal or regulatory requirements. We would recommend that the following additional step be added as requirement R405.15(e):

i. Comply with those requirements, and

ii. Consider reporting the breach to a professional or regulatory body or oversight authority if such reporting is common practice or expected in the relevant jurisdiction.

With respect to proposed paragraph R405.19, we have concerns as the group audit firm’s communication with those charged with governance is not required to be in writing.

The illustrative diagram of the proposed process to address breaches of independence at the component auditor firm contained in Appendix 2 is inconsistent with the proposed requirements relating to breaches contained in Section 405:

a. Proposed paragraphs 405.18 A1 and A2 address the group engagement partner’s determination of whether the breach has been satisfactorily addressed by the component auditor or not before determining whether further action is needed, and the breach is communicated with those charged with governance. The illustrative diagram includes an additional step not contained in Section 405 for the group engagement partner to assess the significance of the breach prior to communicating the breach with those charged with governance.
b. The illustrative diagram distinguishes between a “significant breach” (block I) and a “very significant breach” (block J), yet proposed section 405 does not include the concept of a “very significant breach”.

31. Royal Nederlandse Beroepsorganisatie van Accountants (NBA)

32. New York State Society of CPAs (NYSSCPA)

33. South African Institute of Chartered Accountants (SAICA)

We believe that further considerations need to be made by IESBA in this regard. As mentioned above, some jurisdictional challenges may make it impossible for certain component auditors to comply with the requirements in the Exposure Draft. The application of different independence requirements due to different Ethical Codes being adopted could create challenges for the group engagement team as the component auditors may not be under any obligation to report the potential breaches according to their jurisdictional codes.

Furthermore, the group engagement team may face restrictions to access to information as the component auditors may not be allowed to share relevant information with the group engagement team. The current situation in Ukraine and Russia is case-in-point where the sanctions imposed upon Russia may prevent component auditors in that region from sharing information with group engagement teams that may be located in other jurisdictions. The Exposure draft needs to include provisions that address such situations, generally.

Mandatory Audit Firm Rotation (MAFR) and joint audit requirements could also result in certain challenges in other jurisdictions like South Africa where only a few audit firms may have the expertise and competence to perform specialised audits like large banks and insurers. SMP firms may not have the skills and resources to perform such complex audits, therefore, clients may be forced to engage firms that may not be adequately independent because they may have provided other non-assurance services or be forced to breach MAFR requirements. It is important that the IESBA engages with the local South African jurisdiction in this regard and SAICA would be willing to set up such discussions.

34. South African Institute of Professional Accountants (SAIPA)

We agree with the IESBA that the process to address a breach of an independence requirement at the CA firm level needs to be clarified in the Code.

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.

The IESBA is proposing that the process to deal with a breach at a nonnetwork CA firm follows broadly similar principles as in the process to deal with a breach in the extant Code as per Appendix 2 outlined.

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 nonnetwork 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.

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

35. The Society of Certified Accountants and Auditors of Kosovo (SCAAK)

We agree.

36. Federation of Accounting Professions, Thailand (TFAC)

Yes, we agree.

37. Wirtschaftsprüferkammer (Germany) (WPK)
We agree with the proposals in Section 405 to address a breach of independence by a CA firm.

Firms

38. Association of Italian Audit Firms (ASSIREVI)

Section 405 provides a detailed requirements and guidance to deal with circumstances where a breach of the independence requirements is identified by a CA outside the GA firm’s network.

Assirevi believes that the process itself, as outlined in section 405, is reasonable. We also agree that the evaluation to be performed by the GA should be focused on the impact of the breach upon the objectivity of the CA and thus on the ability of the GA to use the CA’s work for purposes of the group audit.

However, the proposal to apply the same independence provisions to individuals from both the GA firm and non-network CA firms would make it complex to differentiate the evaluation to be performed by the GA when the same breach has occurred within the GA network or at a non-network CA firm.

Assirevi believes that more guidance is required to support the GA in exercising its professional judgment and, in general, adequately documenting and evaluating the independence of the non-network CA firm. This is particularly important as the GA has no knowledge of – or control over – the processes in place to prevent and detect breaches to independence provision at the non-network CA. While, as requested by ISA 600 (Revised), the GA is able to be involved in the CA firm’s audit work and to review the related working paper, when it relates to compliance with independence requirements the GA could only obtain a confirmation from the CA on its commitment and ability to comply. The processes used by an audit firm to manage and monitor compliance with the independence requirements are firm-specific and cannot be disclosed to another audit firm. Once again, the unintended outcome could be a reduced possibility to use non-network CA firms, as in this case the GA will be exposed to the consequences of a potential breach incurred by a non-network CA firm over which it has no control.

39. BDO International Limited (BDO)

BDO agrees with the proposals contained in paragraph R405.14 relating to a breach identified by a component auditor firm with the group auditor firm’s network.

With respect to the proposals relating to a breach identified by a component auditor firm outside the group auditor firm’s network, BDO is of the view that a necessary step for the component auditor firm is missing, namely to consider whether, and appropriately respond to any legal or regulatory requirements. BDO therefore recommends that the following additional step be added as requirement R405.15(e):

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

i. Comply with those requirements, and

ii. Consider reporting the breach to a professional or regulatory body or oversight authority if such reporting is common practice or expected in the relevant jurisdiction.

With respect to proposed paragraph R405.19, BDO questions why the group audit firm’s communication with those charged with governance is not required to be in writing.

While we support the use of visual aids within professional standards, the Illustrative diagram of the proposed process to address breaches of independence at the component auditor firm contained in Appendix 2 is not consistent with the proposed requirements relating to breaches contained in Section 405:

a. Proposed paragraphs 405.18 A1 and A2 address the group engagement partner’s determination of whether the breach has been satisfactorily addressed by the component auditor or not before determining whether further action is needed, and the breach is communicated with those charged with governance. The illustrative diagram includes an additional step not contained in Section 405 for the group engagement partner to assess the significance of the breach prior to communicating the breach with those charged with governance.
b. The illustrative diagram distinguishes between a “significant breach” (block I) and a “very significant breach” (block J), yet proposed section 405 does not include the concept of a “very significant breach”.

40. Deloitte Touche Tohmatsu Limited (DTTL)

When a CA firm within the GA firm’s network identifies a breach:

Deloitte Global agrees that identification of a breach by a CA firm within the GA firm’s network should prompt the application of the provisions in paragraphs R400.80 to R400.89, as per the extant Code. We note that the responsibilities in the proposal are placed on the group engagement partner, while the breach provisions in the extant Code are focused on activities of the firm and the proposal requires immediate communication instead of prompt communication. We recommend aligning the proposed language with the extant Code as follows:

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 promptly communicate the breach immediately to the group engagement partner including actions proposed to address the consequences of the breach. 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 CA firm outside the GA firm’s network identifies a breach:

Deloitte Global generally supports the approach proposed by the Board to address breaches that occur at a CA firm outside the GA firm’s network. However, we propose certain amendments to the provisions to better reflect the respective roles of the CA firm and the GA firm engagement partner in the process. In particular, ISA 600 requires the group engagement partner to take responsibility for the CA firm having been made aware of relevant ethical requirements that are applicable and for confirming whether the CA firm understands and will comply with such requirements. If there has been a breach by a CA firm of the relevant ethical requirements, including those related to independence, and the breach has not been satisfactorily addressed, the group auditor cannot use the work of that CA firm. The group engagement partner should not, however, be required to assess the CA firm’s objectivity, but rather the CA firm’s assessment of the impact of the breach on their objectivity. We suggest the language could be revised as follows:

R405.15

(d) Promptly communicate the breach to the group engagement partner in writing, 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 of the impact of the breach on the component auditor firm’s objectivity 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.

Communication with those charged with governance of the group audit client:

Deloitte Global supports the new requirement for the GA firm to discuss any breaches that occur at a CA firm outside its network with those charged with governance of the group audit client, including the actions proposed or taken to address the consequences of the breach. As per our comment above, we also
recommend that the wording of the provision is amended to emphasize that the assessment of the significance of the breach is performed by the CA Firm, as follows:

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 component auditor firm’s assessment of 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 for the purposes of the group audit.

Such discussion shall take place as soon as possible unless the breach is considered to be less significant and an alternative timing is specified by those charged with governance for reporting less significant such breaches.

41. Grant Thornton International Ltd (GTIL)

GTIL supports the proposals in section 405 to address a breach of independence by a component audit firm.

42. Ernst & Young Global Limited (EY)

Yes, we agree with the proposals in Section 405 to address a breach of independence by a component auditor firm.

43. KPMG IFRG Limited (KPMG)

We agree with the proposals to address a breach.

44. Mazars Group (MAZARS)

45. MNP LLP (MMP)

We agree with the proposals in Section 405 to address a breach of independence by a CA firm. We recommend adding a requirement to obtain concurrence from the group auditor firm when there is judgement applied by a CA firm outside of the group auditor’s network in concluding that a breach has not occurred, including guidance on the steps required to obtain concurrence from the group auditor firm and group engagement partner. This ensures that the group auditor firm is protected from any inadvertent breaches of the IIS with respect to the group audit in the event of differences in opinions in the interpretation of the IIS.

46. PKF International Limited (PKF)

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

47. Pitcher Partners (PP)

Firstly the timing of reporting appears different for an in network and out of network auditor which is conceptually inconsistent. Additionally the PIE rules mean that component auditors could instantly find themselves in breach if they are determined to be a material component.

48. PricewaterhouseCoopers International Limited (PWC)

Yes. The ultimate outcome that is of most relevance is that if those charged with governance do not concur with the group auditor firm’s assessment that the actions proposed or taken satisfactorily address the consequences of the breach, the group auditor firm will be precluded from using the work of the CA firm. That is consistent with the principle and guidance established in ISA 600 (Revised).
Others

49. IFAC Small and Medium Practices Advisory Group (IFAC SMPAG)

Overall, we believe the suggested approach regarding breaches is operable, especially since it refers to these factors that we have raised earlier, such as "evaluate the significance, impact on objectivity" (R405.15 b-c and R405.17) about exercising professional judgment and using the third-party test. However, in relation to the approach taken regarding the actual independence requirement, (i.e., applying the stricter PIE-rules without any distinctions - and motivating this with consistency and perception issues) it seems to be a bit contradictory.

One way to address this issue would be to use the reasoning behind the breaches sections consistently in section 405. As proposed, we believe the guidance appears to be unbalanced.

It was noted from one of our members that the proposals outlined related to a breach of independence by a component audit firms may not be feasible in some jurisdictions. In certain jurisdictions, the law may prohibit accounting firms from communicating internal information to the group auditor firms located overseas. In addition, group audit firms may have to wait until a component audit firms confess the breaches. This is because group audit firms and component audit firms do not use common independence infrastructures as the large firms use. The SMPAG proposes the Board consider whether the focus should be more on the impact the breach had on the work performed and related audit opinion, rather than on the breach itself.