Basis for Conclusions
Prepared by the Staff of the IESBA®
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International Ethics Standards Board for Accountants®

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

IESBA International Ethics Standards Board for Accountants®

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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 Foundation for Ethics and Audit™ (IFEA™).

BASIS FOR CONCLUSIONS:
REVISIONS TO THE CODE RELATING TO THE DEFINITION OF ENGAGEMENT TEAM AND GROUP AUDITS

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I. Introduction

1. At its November–December 2022 meeting, the IESBA unanimously approved the revisions to the provisions of the Code relating to the definition of engagement team and group audits.

2. This Basis for Conclusions is prepared by IESBA staff and explains how the IESBA has addressed the significant matters raised on exposure. It relates to, but does not form part of, the revisions to the Code.

II. Background

Development of Engagement Team – Group Audits Project

Revisions to IAASB's Standards

3. In December 2016, the International Auditing and Assurance Standards Board (IAASB) approved a project proposal[1] to address the revision of ISQC 1,[2] ISA 220[3] and ISA 600.[4]

Changes to the Definition of Engagement Team

4. Among other matters, the IAASB changed the definition of an engagement team (ET) in ISA 220 (Revised)[5, 6] to recognize different and evolving ET structures. In proposing this definitional change, the IAASB considered that ETs 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 determined that individuals who perform audit procedures on the engagement are part of the ET, regardless of their location or employment status, so that their work can be appropriately directed, supervised and reviewed.

5. 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 other individuals in the revised definition, including component auditors, raised several questions concerning compliance with the Code's provisions, given that the definitions of the term in the Code and the ISAs are intended to be aligned.

6. In 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 that the Code's provisions apply to the various individuals who are part of the ET under the revised definition. The IAASB clarified in ISA 220 (Revised) that the independence requirements applicable to members of the ET are specified in relevant ethical requirements, which, as defined in ISA 220 (Revised), include the Code.

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1 Enhancing Audit Quality: Project Proposal for the Revision of the IAASB's International Standards Relating to Quality Control and Group Audits

2 International Standard on Quality Control (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

3 International Standard on Auditing (ISA) 220, *Quality Control for an Audit of Financial Statements*

4 ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

5 ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

6 The IAASB approved ISA 220 (Revised) at its September 2020 meeting, and it was issued in December 2020.

Independence of Component Auditors in a Group Audit

7. Leveraging the progress made on other projects, in particular the revisions of ISQC 1 and ISA 220, the IAASB issued an Exposure Draft of ISA 600 (Revised)[7, 8] in April 2020. Some respondents to that Exposure Draft raised concerns regarding the interactions of the proposed revised definition of ET with relevant ethical requirements, particularly concerning the application of the International Independence Standards (IIS) in Part 4A[9] of the Code, in the context of an audit of the group financial statements.

8. Given that backdrop and the fact that component auditors 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), the IESBA considered that it was necessary for the IIS to provide clear and consistent guidance concerning the independence of component auditors outside the network. Additionally, the IESBA agreed that it was necessary to go beyond individuals included in the ET definition and consider the independence framework applicable to a component auditor firm.

9. During the IESBA's consultation on its Strategy and Work Plan 2019–2023 (SWP), there was also an encouragement for the IESBA to consider a project to address practical issues encountered by group auditors as well as component auditors in applying the 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.

10. As part of its monitoring of the external environment for emerging issues or developments, the IESBA's Emerging Issues and Outreach Committee also identified a few matters relating to the application of the IIS with respect to component auditors. These included the following:

    - The implications when a parent entity is a public interest entity (PIE), but a component is not, and that component is audited by a non-network firm, particularly whether the component auditor would need to follow the independence requirements that apply to audits of PIEs or non-PIEs.
    - The practical implications of a breach of independence at a component auditor and any safeguards if the group auditor still intends to use the component auditor's work (separately from the group auditor's consideration under ISA 600).

Approved Project

11. Given the above background, in March 2020, the IESBA approved a project proposal to review the definition of ET and independence considerations for group audits in the Code.

12. The objectives of the project were 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

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7 ISA 600 (Revised), *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

8 The IAASB approved ISA 600 (Revised) at its December 2021 meeting, and it was issued in April 2022.

9 Part 4A – Independence for Audit and Review Engagements

(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 component auditors outside the group auditor's network.

Exposure Draft

13. In February 2022, the IESBA released the Exposure Draft, *Proposed revisions to the Code Relating to the Definition of Engagement Team and Group Audits* (ED) with the comment period closing on May 31, 2022. As stated in the Explanatory Memorandum (EM) to the ED, the IESBA proposed, among other matters, to:

- Align the definition of "engagement team" in the Code with the definition of the same term in ISA 220 (Revised) and ISQM 1.[10]
- Change the definitions of "audit team," "review team" and "assurance team" to recognize that engagement quality reviewers (EQRs) may be sourced from outside a firm and its network.
- Enhance the provisions regarding independence considerations in a group audit context by proposing a new Section 405 (Group Audits) on independence principles for individuals and firms, and additions of new defined terms to the Glossary. Among other matters, the IESBA proposed in the new Section 405:
    - The principle that the same independence provisions that apply to individuals from the group auditor firm (GAF) and component auditor firms (CAFs) within the GAF's network should apply to individuals carrying out audit work at the component level from CAFs outside the GAF's network.
    - Guidance to deal with an entity becoming an audit client during or after the period covered by the group financial statements on which the group auditor firm will express an opinion.
    - Enhanced guidance on the process to address a breach of an independence requirement at the CAF level.

14. Forty-nine comment letters were received from respondents across a wide range of stakeholder groups, including two Monitoring Group (MG) members,[11] other regulators, national standard setters, professional accountancy bodies, other professional bodies and firms. Respondents generally supported the alignment of the Code's provisions to the revised IAASB standards and the direction of the proposed changes. Respondents also raised specific comments concerning the consequences of the changes and suggested further clarifications to the proposed text.

15. The IESBA revised its proposals to address the significant matters raised by respondents to the ED, taking into account the input provided by the IESBA Consultative Advisory Group (CAG).

[10] International Standard on Quality Management (ISQM) 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

[11] International Organization of Securities Commissions (IOSCO) and International Forum of Independent Audit Regulators (IFIAR)

16. The key revisions to the ED proposals are as follows:

- Clarify and align the definition of the terms "group audit client" and "component audit client" to the extant Code's "audit client" definition (see paragraph 63).[12]
- Clarify the guidance regarding which types of experts are included in the definitions of ET and audit team (see paragraphs 46-50).
- Include new requirements on communication between the GAF and CAF to complement requirements in ISA 600 (Revised) (see paragraphs 75 -77).
- Set out guidance for the determination of the period during which the independence of a CAF outside the GAF's network is required (see paragraph 161).
- Provide a more targeted and proportionate approach for independence considerations applicable to group audit team members within, or engaged by, a CAF outside the GAF's network (see paragraphs 71- 92).
- Provide enhanced guidance regarding the provisions prohibiting a CAF outside the GAF's network from holding financial interests in, and having loans involving, the group audit client (see paragraph 110).
- Clarify requirements for CAFs where the component audit client is not a PIE but the group audit client is a PIE (see paragraph 114).
- Provide guidance where there is a change in CAF or in the group audit client's circumstances (see paragraphs 166-167).
- Enhance the consistency of the process for addressing a breach at CAFs within and outside the GAF's network (see paragraphs 144-145).
- Enhance and clarify the approach to, and content of, the GAF's communication to those charged with governance (TCWG) of the group about any breaches at the CAF level (see paragraphs 155-159).

Coordination with IAASB

17. In developing the revisions and responding to the comments on the ED, the IESBA 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).

III. Definition of Engagement Team

Revision of Engagement Team Definition

18. In considering aligning the definition of ET in the Code with the definition in ISA 220 (Revised),[13] the IESBA recognized that the extant definition of ET in the Code applies to both audit and other

[12] Revised "audit client" and "group audit client" definitions are also provided to align with changes to the definition of audit client arising from the revisions to the definitions of listed entity and PIE in the Code, issued in April 2022.

[13] The revised definition of ET in ISA 220 (Revised) is as follows:

assurance engagements. In contrast, the definition of ET in ISA 220 (Revised) applies only to audit engagements. Therefore, the IESBA agreed that simply substituting the definition of ET in the Code with the revised definition in ISA 220 (Revised) would not be appropriate.

19. However, the IESBA noted that ISQM 1 addresses ETs 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 and internal auditors who provide direct assistance on an engagement."*

20. In light of the above, the IESBA revised the definition of ET in the Glossary of 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.

21. As the concept of an ET in the Code is used only in the case of audit and other assurance engagements, the IESBA agreed to use the generic term "team"[14] in Part 3 of the Code to denote a team of individuals who perform professional services in a broader context.

22. The revision of the ET definition in ISA 220 (Revised) raised several questions concerning compliance by the individuals included in the ET with the IIS, especially in the case of a group audit. Therefore, the IESBA developed independence provisions applicable to the individuals covered in the revised definition, for example, experts and component auditors, considering their roles in the audit engagement and the specific facts and circumstances. These matters are further discussed in Section IV of this document.

23. Respondents to the ED generally supported the IESBA's proposals regarding the alignment with the ET definition in the IAASB's standards.

Determination of Engagement Team and Audit Team

24. Given that members of the ET are also part of the audit team, the IESBA considered the implications of:

- The changes to the ET definition for the definition of audit team; and

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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 and internal auditors who provide direct assistance on an engagement.

(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.

[14] The IESBA did not see a need to define the term "team" in the broader context of the Code given the generic meaning of the term.

- The other recent changes to the IAASB's quality management standards, i.e., ISQM 1 and ISQM 2.[15]

As a result, the IESBA proposed amendments to the audit team[16] definition, complemented by explanatory material in Part 4A to facilitate the consistent determination of ET and audit team members in the context of an audit engagement.

25. Respondents to the ED supported the amendments to the ET and audit team definitions; however, they raised concern that the definitions, especially when read in conjunction with the application material provided in Section 400, were complex. They raised questions regarding whether specific individuals would be ET or audit team members based on their role in the audit engagement. They asked the IESBA to provide further clarification, either as part of application material in the Code or through non-authoritative guidance.

26. The IESBA acknowledged that the definitions of ET and audit team might seem complex because they cover a number of individuals who play different roles in the audit. To assist users of the Code to better understand who is included in the ET and the audit team/group audit team, and in response to the suggestions for further clarifications, the IESBA has developed the diagrams in Appendix 1 and 2 to this document. Complementing the application material added in Section 400 on ET and audit team, the IESBA believes that these diagrams will support the consistent application of the definitions.

27. Furthermore, the IESBA commissioned IESBA Staff to develop Frequently Asked Questions (FAQs) to address questions and requests for clarification from respondents to the ED on whether specific individuals would be part of the ET or the audit team. Apart from the amendments to the ED mentioned below, the IESBA did not add further specificities and examples to the application material as those could lead to an undue amount of detail in the Code relative to other guidance in Section 400.

Engagement Quality Reviewers and Other Audit Team Members

28. During its deliberations, 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 its network. However, consistent with ISQM 2,[17] EQRs[18] 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.

29. The IESBA had agreed 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. Respondents to the ED expressed support for the Code acknowledging that an EQR could also be sourced from outside the firm and network firms and that the EQR should be subject to the same independence requirements as other audit team members.

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15 ISQM 2, *Engagement Quality Reviews*

16 The IESBA also proposed conforming amendments to the definition of "review team" and "assurance team."

17 See ISQM 2, paragraph A4

18 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 scoped in an external individual.)

30. 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 or outside the firm. Similar considerations apply with respect to reviews and other assurance engagements.

31. As such, the IESBA proposed to amend the definitions of "audit team," "review team," and "assurance team" by adding the phrase "or engaged by"[19] to subparagraph (b) of those definitions to include all such individuals.

Independent Service Providers

32. As a result of aligning the proposed definition of ET with the definition of ET in ISQM 1, the IESBA proposed to make it explicit in the application material added in Section 400 that the IIS apply to individuals from service providers who perform audit procedures on an audit engagement, including those outside a firm's network in the context of group audits.[20] In substance, however, including individuals from service providers 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.

33. Although an individual from a service provider would be covered by the IIS, the IESBA did not believe that the scope of the IIS should be extended to cover the organization that provides the human resource (other than in the case of a CAF outside the GAF's network, as discussed below). This is because such an organization does not perform audit work. Accordingly, the IESBA was of the view that it would be disproportionate to bring such an organization into the scope of the IIS.

Comments

34. Although "service provider" is already a defined term in ISQM 1, a few respondents had concerns that it was not clear how this term would be applied in the context of the Code. They also questioned why the application material referenced the definition only partially. They suggested that the Code provide further clarity via specific examples.

35. There were a few comments that the guidance relating to the determination of a service provider referred to both individuals and organizations, which could create the impression that the IIS apply not only to individual service providers who perform audit procedures on an audit engagement but also to the organization that provides the human resource. They felt that the Code should be more explicit about the independence considerations applicable to the individual service provider and the organization that provides the human resource.

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[19] 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.

[20] ISQM 1 defines a service provider as "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."

IESBA Decisions

36. Although ISQM 1 defines "service providers," the application material in Section 400 only focuses on those who perform the audit procedures. Therefore, the IESBA does not believe that it is necessary to include the definition of a service provider from ISQM 1 verbatim. The IESBA also noted that the examples of service providers in ISQM 1 apply in the context of the Code; therefore, no further guidance is necessary in Section 405 in this regard.

37. Regarding the independence considerations for the individual service provider and the organization that provides the human resource, the IESBA noted that the proposed ET definition only includes *individuals* who perform procedures on the engagement. Therefore, the IESBA did not believe it necessary to make it explicit in the Code that the IIS do not apply to the organization that provides the human resource (other than a CAF outside the GAF's network in a group audit as addressed in Section 405).

Experts

38. Similar to the extant ET definition, the revised ET definition explicitly excludes external experts (as well as internal auditors who provide direct assistance on the engagement). 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.

39. 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. By referencing the relevant ISAs in the revised ET definition, the IESBA recognized that ISA 620[21] already addresses the auditor's responsibilities relating to the work of an external expert in obtaining sufficient appropriate audit evidence, including the evaluation of the objectivity,[22] competence, and capabilities of that individual.

40. Nevertheless, the Code recognizes that there are different types of experts, other than external experts as defined in the Code, who might be used on an audit engagement, and depending on the circumstances, they may be members of the ET or the audit team as these terms are defined in the Code. The IESBA had proposed application material in the ED to facilitate the determination of whether such experts are part of the ET or the audit team in the case of an audit engagement.

Comments

41. Respondents generally agreed with the exclusion of external experts and internal auditors who provide direct assistance on the audit from the ET and audit team definitions. However, a few respondents, including a MG member, suggested that the IESBA consider closer alignment with the relevant provisions of ISA 620 regarding the determination of an auditor's expert and responsibility for the work of that expert.

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21 ISA 620, *Using the Work of an Auditor's Expert*

22 ISA 620, paragraph 9, requires that in evaluating the objectivity of an external expert, the auditor make inquiries about interests and relationships that may create a threat to that expert's objectivity.

42. Regarding the experts who are part of the ET or the audit team, there were some comments that further guidance and examples regarding the role of these experts and whether they are part of the ET or the audit team would be necessary.

43. Some respondents questioned whether the proposed changes would sufficiently accommodate the role and independence of experts providing sustainability-related services. They suggested that the IESBA consider the impact of the use of experts in Part 4B of the Code. It was noted that the use of experts providing sustainability-related services is likely to increase with the increase in demand for reporting Environmental, Social and Governance (ESG) information.

44. A few commenters noted that while there was mention of "experts from a CAF" in the application material in Section 400, there were no specific examples of them in the guidance provided. It was also questioned whether individuals engaged as experts by the CAF outside the GAF's network could be audit team members.

45. A few respondents suggested that the IESBA consider introducing some flexibility when the consultation with experts was not significant, for example, adding a threshold based on the time spent on the consultation or the significance of the issue under consultation.

IESBA Decisions

46. Concerning the determination of external experts, the IESBA noted that the Glossary in the extant Code already defines “external experts”[23] as individuals with expertise in fields other than accounting or auditing. To clarify this point, the IESBA agreed to delete the reference to “in fields other than accounting or auditing” in the application material in Section 400. Such reference is unnecessary given that it is specified in the definition of “external expert” in the Glossary. (See paragraph 400.11.)

47. Although external experts are not scoped in for the purposes of the IIS, they are required to have the necessary objectivity under ISA 620 in the context of an audit of financial statements. In line with respondents’ comments, the IESBA refined the reference to ISA 620 in the explanatory material attached to the ET definition in the Glossary to (a) further align the determination of an auditor's expert to the determination in ISA 620, and (b) clarify that ISA 620 deals with the auditor's responsibilities relating to the work of such experts.

48. Regarding the independence of experts providing sustainability-related services, such as sustainability assurance, the IESBA noted that addressing this matter was not within the remit of this project. Instead, at its November-December 2022 meeting, the IESBA agreed to take up the matter as part of a new project addressing the use of experts.

49. Concerning experts within, or engaged by, a CAF, whether within or outside the GAF's network, the IESBA clarified that whether such individuals are members of the ET or audit team depends on their role on the audit engagement. If a CAF engages an expert (other than an external expert) to perform audit procedures for the purposes of the group audit, this individual comes under bullet (a) of the group audit team definition. If an expert (other than an external expert) within a CAF can directly influence the outcome of the group audit, that individual would come under either bullet (c) or bullet

[23] The Glossary defines an “external expert” as an individual (who is not a partner or a member of the professional staff, including temporary staff, of the firm or a network firm) or organization possessing skills, knowledge and experience in a field other than accounting or auditing, whose work in that field is used to assist the professional accountant in obtaining sufficient appropriate evidence.

(d) of the group audit team definition. However, the IESBA did not believe that individuals engaged by a CAF would be able to directly influence the outcome of the group audit as they would be further removed from the group audit; therefore, the IESBA determined that such individuals should not be part of the group audit team. The IESBA amended the application material in Section 400 to clarify some of those distinctions (see paragraph 400.11). The IESBA also agreed to commission IESBA Staff to develop FAQs to explain the application of the definitions in relation to experts in more detail.

50. Regarding the suggestion for a more scalable approach to independence considerations applicable to experts who are consulted on the audit engagement, the IESBA noted that the definition of group audit team already includes an element of proportionality with respect to experts within a network firm or a CAF outside the GAF's network who can *directly influence* the outcome of the group audit engagement. The IESBA believes it would be impracticable to establish quantitative thresholds to scope such individuals as suggested.

IV. Independence Considerations for Group Audits

51. In thinking through independence considerations in a group audit context, the IESBA approached this matter from two different perspectives:

    (a) Independence principles for individuals who are members of the group audit team; and

    (b) Independence principles for firms, within and outside the GAF's network, involved in the group audit engagement.

52. To address the independence considerations for individuals and firms in an audit of group financial statements, the IESBA proposed a new Section 405 (Group Audits) and newly defined terms in the Glossary as further discussed below.

53. There is a difference in the terminology used in ISA 600 (Revised) compared with that used in the new Section 405 in the Code. Specifically, ISA 600 (Revised) sets out requirements for group auditors and component auditors.[24] Section 405 focuses on the independence of GAFs and CAFs, in addition to the personal independence of the individuals participating in the group audit.

54. A few regulators, including a MG member, suggested that the Code clarify in Section 405 which individuals in the CAF are responsible for compliance with the Code's provision. The IESBA noted that paragraph 400.4 (amended as a result of conforming amendments following the issuance of the IAASB's suite of quality management standards in December 2020) explains that many of the provisions of Part 4A of the Code do not prescribe the specific responsibility of individuals within the firm for actions related to independence, instead referring to "firm" for ease of reference. Paragraph 400.4 further states that a firm assigns operational responsibility for compliance with independence requirements to an individual(s) or a group of individuals in accordance with ISQM 1. This general provision regarding the allocation of responsibilities with respect to independence within a firm is also applicable to a CAF, given the applicability of paragraph 400.4 to CAFs pursuant to Section 405. Accordingly, the IESBA determined that no specific changes were needed in relation to this matter.

[24] Paragraph 14(c) of ISA 600 (Revised) defines the component auditor as an auditor who performs audit work related to a component for purposes of the group audit. Paragraph 13(d) of ISA 200 defines the auditor as the person or persons conducting the audit, usually the engagement partner or other members of the engagement team, or, as applicable, the firm.

New Defined Terms

55. For purposes of specifying independence provisions for group audits, the IESBA proposed a set of new defined terms for inclusion in the Glossary to the Code. These definitions are based on or aligned as closely as possible with those in ISA 600 (Revised).

Comments

56. Respondents generally supported the newly defined terms. Commenters raised, among other matters, the following general issues and areas for clarification:

- In relation to alignment with the terms in the ISAs, a few respondents questioned why the new definitions refer to "audit work" while the ET definitions in the Code and ISA 220 (Revised) refer to audit procedures. They asked whether "audit work" captures a broader range of activities.
- There was a question as to whether the reference to the "audit work" in the definitions is limited to purely audit work and excludes review and other assurance work.
- There were comments regarding the use of the word "client" in the new definitions given that the audit is often performed for other stakeholders rather than the entity or its management.

57. Two MG members suggested that the IESBA address some of the complexities related to the definition of a component audit client and whether or not the client is a legal entity. Similarly, a few respondents asked for clarifications regarding the definition of a group audit client and the scope of related entities covered by that definition.

58. The proposed definition of group audit team (audit team for the group audit in the ED) includes individuals within a CAF outside the GAF's network who can directly influence the outcome of the engagement. Some commenters asked the IESBA to provide further guidance with respect to determining individuals "who can directly influence the outcome of the group audit." Some argued that clarification or examples would be necessary as they felt it would be rare that there would be such individuals in a group audit.

IESBA Decisions

59. The IESBA noted that the reference to "audit work" captures a broader range of activities than performing audit procedures. For greater consistency, the IESBA reviewed the use of the terms "audit work" and "audit procedures" in the proposed Section 405 in light of the IAASB's previous discussion[25] in the context of the ISA 600 project.[26, 27]

60. Regarding the question of whether audit work includes review work, the IESBA noted that paragraph 400.2 of the Code states that the term "audit" in Part 4A applies equally to "review." However, the

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[25] See paragraphs 29 and 30 of IAASB September 2021 Meeting, Agenda Item 2, *Proposed ISA 600 (Revised) – Issues Paper.*

[26] The IAASB's position is that "audit work" refers more broadly to the entirety of the work effort, including with respect to the work requested to be performed by component auditors. For example, audit work would encompass all aspects of planning and performing the group audit, including with respect to direction, supervision and review, and necessary administrative tasks (e.g., coordination with management). In the context of ISA 600 (Revised), the IAASB used "audit procedures" when referring more specifically to the nature, timing and extent of audit procedures to be performed, including when component auditors are requested to perform specified audit procedures.

[27] In the context of the work of a CAF, where either "audit procedures" or "audit work" could be appropriate, the IESBA determined to use "audit work" to capture a broader scope of work (for example, in paragraph 405.20 A1).

IESBA clarified that in Section 405, the definitions of a CAF and other terms refer to "audit work" for purposes of the group audit in line with ISA 600 (Revised). A group audit is further defined as an audit of group financial statements. Therefore, the IESBA reaffirmed that the newly defined terms, requirements, and application material in Section 405 are not applicable to review or other assurance engagements, but only to an audit of group financial statements.

61. Concerning the comments raised on the use of the word "client," the IESBA noted that this is an issue of a more general nature and that it was outside the scope of this project. The IESBA is, however, considering addressing the matter as part of its Strategy and Work Plan 2024-2027.

62. Concerning the request for clarification regarding the component audit client definition, the IESBA recognized that there is some unavoidable complexity in the definition, given that it needs to focus on legal entities for purposes of the Code's independence provisions. Meanwhile, ISA 600 (Revised) contemplates that a component might be not only a legal entity, but also a business unit, function or business activity. The IESBA determined to clarify this by way of FAQs to be developed by IESBA Staff.

63. In relation to the definition of group audit client and the related entities included within the client, in line with the approach taken in extant paragraph R400.20 regarding related entities included with the audit client, the IESBA determined to make some refinements to the Glossary definition of group audit client to clarify the related entities included when the group audit client is a listed entity and when it is not a listed entity. In addition, the IESBA determined to add below the definition of audit client in the Glossary a reference to the definition of group audit client in the context of a group audit, and below the definition of group audit client, a reference to extant paragraph R400.20. This clarifies that despite the inclusion of related entities in the audit client definition, this term is applicable only in the context of audits of standalone financial statements.

64. Concerning the comments regarding individuals from a CAF outside the GAF's network who can directly influence the outcome of the group audit, the IESBA did not believe that it would be appropriate to provide specific examples of such individuals in the Code. The IESBA is of the view that whether there is direct influence on the outcome of the group audit will depend on the specific facts and circumstances. The IESBA, however, commissioned IESBA Staff to develop an FAQ on this matter.

Independence Considerations for Individuals

Independence of Individuals Within the Group Auditor Firm's Network

65. The extant Code already addresses the personal independence requirements with respect to an audit client. Individuals from a CAF within the GAF's network who participate in the audit of a component are effectively required to comply with the same personal independence requirements that apply to the ET at the GAF.[28]

66. Respondents to the ED generally supported the proposals for group audit team members within, or engaged by, the GAF and its network firms. (See paragraph R405.5.)

[28] Paragraph R400.51 of the extant Code states that "A network firm shall be independent of the audit clients of the other firms within the network as required."

Independence of Individuals Outside the Group Auditor Firm's Network

67. The change in the definition of ET in ISA 220 (Revised) resulted in a need to clarify the independence requirements for individuals within, or engaged by, a CAF outside the GAF's network. In particular, the IESBA had considered whether individuals from a CAF outside the GAF's network performing work on a component for the group audit should be subject to the same personal independence requirements as individuals from the GAF and its network firms.

68. Given that the expanded definition of ET captures all individuals who perform audit procedures irrespective of whether they are from the GAF's network, the IESBA proposed in the ED 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.

Comments

69. In relation to the group audit team members within, or engaged by, a CAF outside the GAF's network, regulatory respondents did not raise significant concerns regarding the approach proposed in the ED. However, a few respondents from the firms and professional bodies pointed out that while the CAF outside the GAF's network has to be independent only of the component audit client (see below in paragraph 96), the CAF still has to monitor its individual audit team members across all the related entities and other components within the group audit client. They felt that this would be overly burdensome. They expressed concerns that a CAF outside the GAF's network may not have sufficient information about all the entities in the group, especially entities that are outside the chain of control of the component audit client. Therefore, they argued that CAFs outside the GAF's network might not be able to monitor the independence of individuals with respect to all entities in the group. They asked the IESBA to consider a more balanced approach focusing only on relationships with entities more likely to threaten the individuals' independence.

70. In this regard, some respondents questioned whether it is necessary that individuals within, or engaged by, the CAF outside the GAF's network who are involved in the group audit be independent of the related entities of the group audit client, especially parent and sister entities for a group audit client that is a listed entity.

IESBA Decisions

71. Firms within the same network share common characteristics and a common system of quality management, including a system for monitoring independence. The Code also requires a network firm to be independent of any audit clients of other firms within the network. Therefore, CAFs within the GAF's network come within the ambit of the network's system for monitoring independence and, through the network, are provided with sufficient and timely access to information about the group audit client and its related entities and other components to enable them to meet the independence requirement under the Code. However, CAFs outside the GAF's network will not have access to the network's system for monitoring independence. The IESBA therefore acknowledged the concerns about potential practical challenges CAFs outside the GAF's network might face in monitoring the independence of their group audit team members with respect to all related entities and other components within a group audit client, especially in the case of very large, multinational group audit clients. The IESBA considered that there was potential for the cost of implementing a system to monitor compliance with such independence requirements at a CAF outside the GAF's network to

become disproportionate relative to the likelihood of threats created. In addition, the IESBA recognized that if the CAF outside the GAF's network had to monitor the independence of individuals with respect to all entities within the group audit client, this could become a significant compliance task, especially for large groups. The unintended consequence would be to take resources and time away from the CAF's focus on the audit work, potentially adversely impacting audit quality.

72. Given these concerns, the IESBA reconsidered whether it is necessary to scope in all related entities within the group the same way when determining the personal independence of the group audit team members, given that the likelihood of threats to independence will vary depending on the distance of the related entities from the component audit client. The IESBA noted that in the context of a group audit, the greatest threats to independence lie with respect to the component audit client[29,30] and the entity on whose group financial statements the GAF expresses an opinion. Therefore, it is appropriate that the Code require all group audit team members, irrespective of whether they are within or outside the GAF's network, to be independent of these entities in accordance with Part 4A of the Code. (See paragraph R405.6(a) and (b).)

73. The IESBA also acknowledged that any relationship or circumstance between an audit team member within, or engaged by, a CAF outside the GAF's network and a controlled entity of the group audit client in the "chain of control" of the component audit client could also compromise the group audit team member's independence with respect to the component audit client. Therefore, the IESBA determined to also require group audit team members from a CAF outside the GAF's network to be independent of such entities in accordance with Part 4A. The IESBA believes that this option would strike an appropriate balance between how far to scope in related entities of the group audit client and the associated compliance burden as it would exclude a potentially large number of entities controlled by the group audit client that are not part of the chain of control of the component audit client. (See paragraph R405.6(c).)

74. Regarding any other related entities and components within the group audit client, the IESBA noted that even if the Code did not require group audit team members within, or engaged by, CAFs outside the GAF's network to comply with the provisions of Part 4A in relation to these other related entities and components, this would not mean that a CAF outside the GAF's network should not consider and address any threats created by any relationship or circumstance involving its group audit team members with those other related entities and components. The CAF outside the GAF's network would still be required to apply the "reason to believe" principle and include such a relationship or circumstance when identifying, evaluating, and addressing threats to the CAF's independence (see paragraph R405.7 of the ED).

75. In this regard, responding to some of the concerns raised regarding the practical challenges to monitoring personal independence across the group audit client, the IESBA agreed to introduce new requirements in Section 405 to promote communication between the GAF and CAFs, leveraging the communication requirement in ISA 600 (Revised).

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[29] This is because the individual from the CAF outside the GAF's network would be performing audit procedures at the component audit client and that would impact the group financial statements. However, the individual would not be involved in performing procedures on, or evaluating the results of that audit work with respect to, the other related entities and other components within the group audit client.

[30] The definition of component audit client also includes any entities over which the client has direct or indirect control.

76. With reference to the specific responsibility of the group engagement partner under ISA 600 (Revised) to make a component auditor aware of the relevant ethical requirements that are applicable given the nature and circumstances of the group audit engagement,[31] the IESBA added a requirement calling on the GAF to communicate at appropriate times the necessary information to enable the CAF to meet its responsibilities under Section 405. Application material to the requirement provides specific examples of matters the GAF might communicate, including any related entities and other components within the group audit client that are relevant to the independence considerations applicable to the CAF and the audit team members within, or engaged by, that firm. (See paragraphs R405.3 and 405.3 A1.)

77. The IESBA also noted that ISA 600 (Revised) requires[32] the group auditor to request the component auditor to communicate whether the component auditor has complied with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement. As part of the new subsection on communication between a GAF and a CAF, the IESBA determined to explicitly require that the CAF's communication include (see paragraph R405.4):

- Any independence matters that require significant judgment; and
- In relation to those matters, the CAF's conclusion whether the threats to its independence are at an acceptable level, and the rationale for that conclusion.

Further consideration of practical challenges

78. Regarding the practical challenges in relation to monitoring personal independence across the group audit client by the CAF outside the GAF's network, a few stakeholders and the PIOB suggested during further outreach post-exposure that the IESBA should better understand and evidence the practical challenges before proposing to move away from the approach in the ED. They argued that based on the requirements of ISA 600 (Revised), the group engagement partner and the GAF need to be aware of all the entities within the group and should be able to communicate such information to the CAFs. They were concerned that the revised approach could create a perception of a "lower" level of independence for group audit team members within, or engaged by, a CAF outside the GAF's network. There was also a concern that the approach of using the "reason to believe" principle could risk an inconsistent application of the independence requirements.

79. Regarding evidencing the actual practical challenges related to the ED proposal, the IESBA first considered the circumstances in which a GAF would ordinarily decide to involve firms outside its network in the group audit. As data on group audits at a global level are not readily available, the IESBA considered the regulations and practices relevant to group audits and the size of entities to which those regulations and practices usually apply. Although there is a wide range of types and sizes of group audits, the IESBA believes that group audits usually only involve CAFs outside the GAF's network when the group audit client is a larger multinational conglomerate with components worldwide.

80. In the case of a group audit client with few related entities and other components, the GAF may well communicate information about all the related entities and other components to the CAF pursuant to the requirement in paragraph R405.3. In such a case, it is unlikely that there would be an undue

[31] Paragraph 25(a) of ISA 600 (Revised)

[32] Paragraph 45(c) of ISA 600 (Revised)

burden for the CAF to monitor the independence of its group audit team members across the group audit client. However, in large multinational conglomerates, potentially with multiple listed entities amidst hundreds of related entities and other components, providing information about all the related entities and other components could inundate the CAF. Further, given that a component might be a business unit, function or business activity, the entities included with the group audit client might not fall within the related entity definition.

81. Consequently, the IESBA concluded that communication of information about all the related entities and other components to the CAF outside the GAF's network would not eliminate the CAF's burden of processing and analyzing the raw data, especially if mergers, acquisitions or disposals occur regularly within the group.

82. The IESBA considered on due reflection that there are potentially two options for an individual to determine their independence in the group audit context:

    (a) Based on the list of all the related entities and other components of the group audit client, they could assess in relation to each related entity or other component whether there are any relationships or circumstances that would impact their independence ("top-down" approach); or

    (b) Based on the individual assessing whether they have any relationships or circumstances addressed by the IIS, and considering whether any such relationships or circumstances are tied to any related entity or other component of the group audit client ("bottom-up" approach).

    The IESBA believes that under both options, the proper application of the Code and the conceptual framework should lead to the same outcome regarding the individual's independence in the context of the group audit.

83. However, in the case of Option (a) above, the administrative burden from both the GAF's and CAF's perspectives could be disproportionate for a large multinational, multi-industry group relative to the likelihood of threats to independence in related entities and other components of the group audit client outside the chain of control of the component audit client. Importantly, as mentioned above, the IESBA was concerned about the potential unintended consequence of this process becoming a "tick-box" compliance exercise that would draw time and attention of the group audit team members within, or engaged by, the CAF outside the GAF's network away from their focus on addressing the significant risks in the component audit, which would be detrimental to audit quality.

84. Given these considerations, the IESBA determined that Option (b) would provide a more thoughtful approach to independence with respect to these related entities and other components within the group audit client. Under this "bottom-up" approach, a member of the group audit team within, or engaged by, a CAF outside of the GAF's network would be required to notify the CAF of any relationship or circumstance the individual knows, or has reason to believe, might create a threat to the individual's independence in the context of the group audit (see paragraph R405.7).

85. To facilitate consistent application of this requirement by group audit team members within, or engaged by, the CAF outside the GAF's network, the IESBA determined to include illustrative guidance regarding the types of relationships or circumstances involving an individual or any of the individual's immediate family members, as applicable, that the individual might consider when complying with this requirement. The illustrative list of relationships or circumstances set out in the

guidance is based on the independence requirements in Part 4A of the Code applicable to audit team members (see paragraph 405.7 A1).

86. The IESBA also reaffirmed that the "reason to believe" principle is a well-established principle in the Code that already applies to individuals and firms in other requirements.[33] Further, the Code requires professional accountants to have an inquiring mind and exercise professional judgment.[34] In the context of a group audit and the application of the "reason to believe" principle, an understanding of the facts and circumstances, including any interests and relationships that might compromise independence, is a prerequisite. Having an inquiring mind also involves:

    (a) Considering the source, relevance and sufficiency of information obtained, taking into account the nature, scope and outputs of the professional activity being undertaken; and

    (b) Being open and alert to a need for further investigation or other action.[35]

    Consequently, group audit team members must understand their particular relationships and circumstances and whether those would require consideration under the IIS as concerns the group audit client.

87. The IESBA therefore concluded that this approach better achieves the desired outcome by focusing the attention of the group audit team members on the actual relationships or circumstances that could create a threat to their independence.[36]

88. Once the group audit team member has made the notification required by paragraph R405.7, the IESBA determined to require the CAF to evaluate and address any threats to independence created by the individual's relationship or circumstance (see paragraph R405.8). Given the application of the conceptual framework, if the CAF outside the GAF's network cannot reduce the threats to an acceptable level, the individual cannot serve as a member of the group audit team at the CAF.[37]

89. Paragraphs R405.7 and 405.7 A1 would also be applicable to independent service providers engaged by a CAF outside the GAF's network to perform audit procedures for the group audit.

90. Finally, the communication requirement from the CAF to the group engagement partner in paragraph R405.4 would also be applicable to any independence matters regarding group audit team members within, or engaged by, a CAF outside the GAF's network arising from the application of paragraphs R405.7 and R405.8. In addition, in response to feedback from the PIOB, the IESBA determined to make clear that, ultimately, in accordance with ISA 220 (Revised),[38] it is the responsibility of the group

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33 For example, the requirements in paragraphs R220.8, R220.9, R270.3 and R400.20

34 Paragraph R120.5

35 Paragraph 120.5 A1

36 Under this revised approach, if, for example, a group audit team member's immediate family member is a full-time teacher and is not employed in any roles where they influence financial statements, Section 521 of the Code would not be applicable to the assessment of the group audit team member's independence with respect to the group audit no matter which entities are in the corporate tree. However, if the immediate family member is in a financial reporting oversight role, the group audit team member is expected to consider whether that employment relationship is with any entity in the group. Likewise, in applying the "reason to believe" principle, the group audit team member would consider each of the other illustrative types of relationships or circumstances set out in the guidance in paragraph 405.7 A1.

37 Paragraph R120.10

38 Paragraphs 18 and 21 of ISA 220 (Revised)

engagement partner to determine whether independence requirements have been fulfilled for purposes of the group audit (see paragraph 405.4 A1).

91. Overall, the IESBA believes that this revised and better-targeted approach concerning independence for group audit team members within, or engaged by, CAFs outside the GAF's network will result in the same independence outcome as the approach proposed in the ED, but do so in a more operable and proportionate manner, with a lower likelihood of unintended consequences for audit quality, and thus better serve the public interest.

92. Appendix 3 to this document includes an illustration of the approach to independence for group audit team members within, or engaged by, CAFs outside the GAF's network.

Independence Considerations for Firms

Independence of Component Auditor Firms Within the Group Auditor Firm's Network

93. The EM to the ED explained that new independence provisions applicable to the GAF and CAFs within the GAF's network were not necessary 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 proposed the following two requirements in proposed Section 405:

- With respect to the GAF, a requirement to be independent of the group audit client in accordance with the requirements of Part 4A that are applicable to the firm.
- With respect to CAFs within the GAF's network, a requirement to be independent of the group audit client in accordance with the requirements of Part 4A that are applicable to network firms.

94. Respondents to the ED generally supported the proposed requirements above. (See paragraphs R405.9 and R405.10.)

Independence of Component Auditor Firms Outside the Group Auditor Firm's Network

95. The key matter the IESBA addressed in developing the ED was to establish principles applicable to firm independence concerning the CAF outside the GAF's network. The IESBA considered that in the case of a CAF outside the GAF's network, the greatest threat to independence lies with respect to the component audit client where the CAF carries out the audit procedures. The IESBA was of the view that it would be disproportionate and potentially unduly limit the supply of firms able to act as a CAF if the same independence provisions that apply to the GAF's network firms also applied to CAFs outside the GAF's network with respect to all related entities and other components within the group audit client.

96. Taking this into consideration, the IESBA proposed the following independence principles for a CAF outside the GAF's network:

- First, the CAF needs to be independent of the component audit client (as proposed to be defined in the Glossary) consistent with the independence provisions in Part 4A that apply to a firm with respect to its audit client.
- A CAF outside the GAF's network must not hold a direct or material indirect financial interest in, or have loans and guarantees involving, the entity on whose group financial statements the GAF expresses an opinion.

- In the case of other related entities and components within the group audit client, a CAF outside the GAF's network must apply the conceptual framework based on the "reason to believe" principle to identify, evaluate and address any threats to independence.
- With respect to relationships or circumstances involving firms within the CAF's *network* and the component audit client or the group audit client, the CAF must also apply the conceptual framework based on the "reason to believe" principle to identify, evaluate and address any threats to independence.

97. In deliberating the applicable principles for CAFs outside the GAF's network, the IESBA also considered the approach of the extant Code that differentiates the independence provisions applicable to PIEs from those applicable to non-PIEs. The IESBA noted that the purpose of the group audit is to report on the group financial statements and accordingly, the independence provisions that apply at the group level should apply consistently and uniformly across the group. This approach is in line with the overarching principles of ISA 220 (Revised) and ISA 600 (Revised). Consequently, when the group audit client is a PIE and the component audit client is not a PIE, the IESBA proposed in the ED that the independence provisions that apply to the CAF outside the GAF's network in relation to the component audit client be the PIE provisions. Conversely, when the group audit client is a non-PIE, the independence provisions that apply to the CAF outside the GAF's network 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.

Comments

98. Most respondents supported the proposed proportionate approach regarding the independence provisions for CAFs outside the GAF's network. In relation to the independence of the CAF outside the GAF's network, a few respondents raised that the CAF should be independent of the group audit client (including the relevant related entities and other components) regardless of whether the CAF is part of the GAF's network.

99. Regarding the proposed prohibitions in relation to the entity "on whose group financial statements the group auditor firm expresses an opinion," a few respondents noted that the term used to denote this entity would need to be clarified to relate to the ultimate parent entity or at least the top company in the group to prepare group financial statements. Furthermore, there were a few questions about whether the relevant requirements and application material on financial interests in Section 510 apply and how CAFs should determine material and immaterial indirect financial interests.

100. A few respondents, including a MG member, had concerns about the practical challenges related to the application of the proposed "reason to believe" principle in paragraphs R405.7 and R405.8 in the ED. They suggested that the Code include a requirement for the CAF outside the GAF's network to perform inquiries or other procedures within the CAF's network to identify whether a threat to its independence exists.

101. Some respondents were of the view that the CAF should inform the group auditor/group engagement partner if the "reason to believe" principle led to the identification of any threats to the CAF's independence.

102. Although there was support for the proportionate approach proposed for CAFs outside the GAF's network, respondents provided the following comments on the application of the relevant provisions depending on whether the group audit client is a PIE or a non-PIE.

103. For ease of applicability, a few regulatory respondents were of the view that the independence provisions for PIE components within non-PIE groups should be in accordance with those ethical requirements that are most stringent for both the audit of the standalone financial statements of the PIE components and the performance of the group audit. There was a suggestion for reconsidering the proposal, given that the CAF, as a statutory auditor, would already be subject to PIE provisions in such situations.

104. A few commenters also suggested revisiting the wording of the requirement setting out the application of non-PIE provisions to PIE components for the group audit purposes (paragraph R405.9 in the ED) so as not to imply that it is unacceptable for a CAF of a PIE component to apply independence provisions for PIEs when the group is a non-PIE. They argued that it should still be possible to apply more stringent provisions.

105. In relation to the proposal that a CAF outside the GAF's network apply the PIE provisions where the group audit client is a PIE but the component audit client is a non-PIE (paragraph R405.10 in the ED), some respondents raised that the proposed requirement did not consider aspects such as the size or complexity of the component audit client or the extent of work performed by the CAF. They believed that not taking into account the materiality of the components would mean that firms might end up monitoring independence with respect to immaterial components. There were also concerns that applying PIE requirements could raise practical challenges, such as timing in relation to providing a non-assurance service (NAS).

106. Given these concerns, several respondents were of the view that requiring a CAF outside the GAF's network to apply the PIE independence provisions in these circumstances would be unduly burdensome. They suggested that the IESBA consider a proportionate approach that recognizes the relative significance of the component to the group audit and the ability of the CAF's work to directly influence the outcome of the group audit.

107. It was also raised that the Code should clearly state which PIE requirements apply to a CAF outside the GAF's network when the component audit client is a non-PIE and the group audit client is a PIE. There were questions whether these would include the prohibition of certain NAS and the long association provisions. It was also argued that the Code should also explicitly state which PIE requirements would not extend to CAFs outside the GAF's network, such as obtaining the concurrence of TCWG with respect to NAS, or fee disclosure, both of which are focused on a firm and its network firms.

IESBA Decisions

108. After considering the comments on the ED, the IESBA reaffirmed that in the case of a CAF outside the GAF's network, the greatest threats lie with respect to the component audit client and the entity on whose group financial statements the GAF expresses an opinion. The IESBA did not believe that there were compelling reasons put forward by respondents suggesting the need to reconsider this approach. (See paragraph R405.11(a).)

109. Regarding the phrase the "entity on whose group financial statements the GAF expresses an opinion," the IESBA noted that it is only referring to the group audit client without the related entities

or other components.[39] This is because the phrase is referring to "*the entity*." The IESBA believes that this determination is in line with the definition of group audit client in the Glossary, which focuses on the entity on whose group financial statements the GAF conducts an audit engagement. That definition then explains the scope of the related entities included with the group audit client. Therefore, the IESBA did not believe that further explanation or clarification in the Code or the Glossary would be necessary.

110. Concerning the prohibition from holding a financial interest in the entity on whose group financial statements the GAF expresses an opinion, the IESBA agreed to explicitly align this requirement to extant requirements in Section 510 relevant to a firm holding a financial interest in an audit client, a financial interest held as a trustee, and a financial interest received unintentionally with respect to the entity on whose group financial statements the GAF expresses an opinion. (See R405.11(b).)

111. Regarding the application of the "reason to believe" principle with respect to network firms of the CAF, the IESBA considered, in line with the approach applicable to individuals above, that requiring a CAF outside the GAF's network to perform further inquiries or other procedures within its *network* would create a significant administrative burden that would be disproportionate relative to the likely significance of the threats created by relationships or circumstances between the CAF's *network firms* and the component audit client or group audit client.

112. The IESBA also noted that the requirements introduced on the communication between the GAF and the CAF would support the appropriate application of the "reason to believe" principle in the context of Section 405, and the communication about any threats to independence identified as a result.

113. In relation to whether a CAF outside the GAF's network should apply PIE or non-PIE provisions depending on whether the group audit client is a PIE, the IESBA reaffirmed that, as a principle, the independence provisions that apply at the group level should apply throughout the group, including to CAFs outside the GAF's network. While the IESBA has made refinements to bring greater specificity to the application of the principle where the group audit client is a PIE, it did not believe the principle was fundamentally flawed.[40]

114. Consequently, if the group audit client is a non-PIE, the IESBA believes it is appropriate to expect a CAF outside the GAF's network to comply with the provisions applicable to non-PIE audit clients for purposes of the group audit, notwithstanding that the component audit client might be a PIE. Nevertheless, the IESBA noted that if the CAF also performs an audit engagement for a PIE component for reasons other than the group audit, for example, a statutory audit, the CAF must apply the provisions relevant to that other audit engagement, which may be the PIE provisions in the case of a statutory audit. The IESBA determined to provide guidance in paragraph 405.15 A1 to clarify this point.

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[39] In Appendix 3, the entity on whose group financial statements the GAF expresses an opinion is illustrated by *Group Audit Client "A."*

[40] In relation to this general principle, the IESBA also clarified that if the group audit client (the entity under group audit) is a PIE or non-PIE based on national laws, that distinction at the group level should flow to the component level for the group audit purposes, regardless of whether the entity at the component level would be regarded as a PIE by national laws in that entity's jurisdiction. In addition, for group audit purposes, a CAF is required to be independent of the component audit client following the Code's relevant provisions, along with national requirements applicable to the group audit client (the entity under the group audit). The IESBA underlined that the requirements on enhanced communication would assist the GAF in making a CAF aware of the relevant national requirements applicable in the GAF's jurisdiction.

115. The IESBA discussed the comments advocating for a more proportionate approach regarding the application of the PIE provisions, considering the significance and size of the component. However, the IESBA noted that the provisions in the ED are consistent with ISA 600 (Revised), which requires[41] the group auditor to determine the components at which audit work will be performed. ISA 600 (Revised) does not distinguish between components based on considerations such as significance or size. Once the group auditor has determined that audit work will be performed at a component, that component is within the scope of the group audit from a quality management standpoint. Accordingly, the IESBA reaffirmed that the same independence principles should apply to CAFs carrying out audit work at components.

116. However, if the group audit client is a PIE, the IESBA agreed that a CAF outside the GAF's network would only be required to comply with certain independence provisions applicable to a PIE for purposes of the group audit. The IESBA determined that such independence provisions only include:

- The requirements and application material relevant to the permissibility of a NAS to an audit client (see further discussion immediately below), excluding the provisions addressing communication with TCWG of the group audit client on the provision of a NAS (see paragraphs R405.16 and R405.17); and
- The requirements and application material relevant to key audit partners and partner rotation (see paragraph R405.18(b)(ii)).[42]

Non-Assurance Services

117. During the IESBA's discussions on the proposed requirements in the ED, the IESBA considered that it would be useful to clarify the application of the revised NAS provisions for a CAF outside the GAF's network in a group audit context, especially given that the NAS revisions have been substantive. Accordingly, the IESBA proposed guidance in Section 405 to highlight some important considerations when applying the NAS provisions. The IESBA in particular proposed some illustrations of the provision of specific NAS by a CAF outside the GAF's network in the context of a group audit. For instance, the IESBA felt it important to explain how the self-review threat prohibition[43] in the revised NAS provisions should be applied in circumstances where a CAF outside the GAF's network performs limited scope work for purposes of the group audit, for example, audit work limited to a specific line item such as inventory.[44]

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41 Paragraph 22(a) of ISA 600 (Revised)

42 This means that a CAF outside the GAF's network that performs audit procedures at a non-PIE component of a PIE group audit client is not required to apply any other provisions relevant to PIE audit clients, for example, the fee-related provisions in the Code applicable to a PIE audit client.

43 Paragraph R600.16 of the revised NAS provisions

44 In such circumstances, the reference point for the CAF in evaluating the self-review threat that might be created by the CAF's provision of a NAS to the component audit client is the financial information on which the CAF 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.

Comments

118. A substantial body of respondents supported the inclusion of application material on the provision of NAS by a CAF outside the GAF's network to a component audit client, aligned to the revised Section 600. They found the proposed application material sufficiently clear and appropriate.

119. There were a few comments that the application material in the ED (paragraphs 405.12 A1 and A2) was not sufficiently explicit that the application of the requirements of Section 600 should be viewed from the perspective of the component audit client and not the group audit client.

120. Concerning the identification and evaluation of the level of the self-review threat (paragraph 405.12 A2 in the ED), a few regulatory respondents suggested clarifying that the CAF should consider not only the threat in relation to the accounting parts that are subject to the CAF's audit, but also the overall significance of the financial statement line item in the group financial statements.

121. A few respondents also suggested that the Code should provide transitional provisions to address any NAS provided by a CAF outside the GAF's network that may become prohibited under the revised requirements.

IESBA Decisions

122. As explained in paragraph 116 above, the IESBA determined to make some amendments to the structure of the subsection on "Independence Considerations Applicable to Component Auditor Firms Outside a Group Auditor Firm's Network." These amendments emphasize that in the case of a PIE group audit client, the CAF performing audit work at a non-PIE component must apply the PIE provisions of Section 600 for the group audit purposes (except for the requirements on communication with TCWG). (See paragraphs R405.16 and R405.17.) If the group audit client is not a PIE, the CAF is only required to apply the provisions of Section 600 for non-PIE audit clients (see paragraph R405.15).

123. The IESBA also clarified that the application material on the provision of NAS by a CAF outside the GAF's network is applicable with respect to the component audit client (see paragraph 405.16 A1). In line with paragraph R405.11, a CAF outside the GAF's network is not required to be independent of the group audit client with respect to Section 600. However, the proposed Section 405 still requires the CAF to apply the "reason to believe" principle when that firm or its network firm provides any NAS to the group audit client (see paragraphs R405.12 and R405.13).

124. During its deliberations, the IESBA considered whether there might be an issue of perception if the Code did not require a CAF outside the GAF's network to apply the provisions of Section 600 with respect to the group audit client or any parent entities of the component audit client. After due reflection, the IESBA reaffirmed that the proportionate approach proposed in the ED regarding the independence considerations applicable to a CAF outside the GAF's network remained appropriate. As a substantial body of respondents had supported this proportionate approach, the IESBA did not believe there were compelling reasons to revisit this approach. Furthermore, the IESBA noted that Section 600 already provides an exception for any parent entities of an audit client relative to prohibited NAS provided that the NAS do not create a self-review threat.[45] The IESBA was of the

[45] Paragraph R600.26 of the Code

view that the provisions for CAFs outside the GAF's network in the context of NAS are in line with that approach in Section 600.

125. Regarding the comments on the identification and evaluation of the level of a self-review threat at a CAF, the IESBA noted that in line with the provisions in Section 600, a CAF outside the GAF's network would not be able to evaluate a self-review threat that might be created by the provision of a NAS to the component audit client in relation to the group financial statements. Therefore, the IESBA did not believe that it would be appropriate to require a CAF outside the GAF's network to also consider the self-review threat in the context of the group financial statements.

126. Finally, the IESBA agreed to include transitional provisions to address any NAS provided by a CAF outside the GAF's network that may become prohibited under the revised requirements, especially if the group audit client is a PIE. See Section VI, *Effective Date.*

Key Audit Partners

127. During its deliberations of the proposals in the ED, the IESBA considered clarifying how the concept of a key audit partner in the Code applies in the context of a group audit. To highlight the relevance and linkage of the "key audit partner" concept to a group audit, the IESBA proposed guidance in Section 405 to explain that a group engagement partner 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. This would be the case when the individual makes key decisions and judgments on significant matters with respect to the audit of the group financial statements.

128. To further strengthen the linkage with ISA 600 (Revised), the IESBA also proposed an amendment in the ED to the definition of key audit partner to 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.

Comments

129. Respondents supported that the proposals addressed the independence considerations applicable to key audit partners at a CAF and the proposed changes to the definition of a key audit partner in the Glossary.

130. Regarding the proposed application material in Section 405, a few respondents suggested that the Code instead require the group engagement partner to assess whether any engagement partners at the component level can make key decisions and, if so, qualify them as key audit partners and give them proper notice in this respect.

131. A few other commenters were of the view that the proposed application material was not in line with the extant Code's provisions on the ground that the extant Code does not require the determination of who is a key audit partner. They suggested instead that the Code include a determination of who is a key audit partner in a group audit context and require that individual to comply with the relevant provisions in the Code.

IESBA Decisions

132. The IESBA considered that only the group engagement partner has the necessary information to determine whether an audit partner at a CAF who performs audit work for purposes of the group audit is a key audit partner for the group audit. In that context, the determination differs from the

determination of a key audit partner for an audit of standalone financial statements where the audit firm has the necessary information to apply the definition of a key audit partner. Consequently, the IESBA agreed to elevate the application material to a requirement and explicitly state that determining who is a key audit partner at a component level for the group audit purposes, and communicating that determination to the relevant individuals, are the group engagement partner's responsibilities. (See paragraph R405.18(a).)

133. In line with the changes the IESBA determined to introduce regarding communication between a GAF and a CAF, the IESBA also added a requirement for the group engagement partner to specify certain independence requirements that would apply to the individuals at the CAFs who are determined to be key audit partners for the purposes of the group audit. (See paragraph R405.18(b).)

134. In this regard, for purposes of Section 540 addressing long association, an individual who is determined to be a key audit partner at a CAF would be an "other key audit partner" in the context of the group audit. Therefore, in the case of a group audit client that is a PIE, that individual would need to consider paragraphs R540.5(c) and R540.20, and by reference, all the other relevant provisions in Section 540. (See paragraph R405.18(b)(ii).)

Breaches of Independence in Context of Group Audits

135. In developing the ED, one area that the IESBA believed needed to be clarified in the Code was the process of addressing a breach of an independence requirement at the CAF level. The IESBA noted that the extant Code already sets out a process for a firm when it concludes that a breach of a requirement of the IIS has occurred. In the ED, the IESBA proposed requirements and guidance in Section 405 to deal with circumstances where a breach is identified at the CAF, within or outside the GAF's network.

Breaches at a Component Auditor Firm

136. 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. Therefore, in the ED, the IESBA proposed different actions for a CAF within or outside the GAF's network.

137. One of the practical issues the IESBA took into consideration when dealing with breaches at a CAF outside the GAF's network is that it would not be practicable for the GAF to implement the monitoring and disciplinary procedures necessary to ensure the CAF's compliance with all applicable independence requirements for the group audit, given that the CAF is outside the GAF's control.

138. The IESBA proposed that the process to deal with a breach at a CAF outside the GAF's network follow broadly similar principles as in the process to deal with a breach in the extant Code, with the modifications necessary with regard to the nature of the CAF's work for the group audit purposes. Thus, in the event of a breach at the CAF level, the IESBA proposed in Section 405 that the CAF take a number of actions, including communicating the breach to the group engagement partner together with an assessment of the significance of the breach and any actions to address the consequences of the breach. The group engagement partner would then need to assess the breach, focusing on the impact of the breach on the CAF's objectivity and the GAF's ability to use the work of the CAF for purposes of the group audit before deciding on the need for any further action.

139. The ED set out guidance to make clear that in some circumstances, the group engagement partner might determine that additional actions are needed beyond the CAF's actions to satisfactorily remedy the breach to enable the GAF to use the CAF's work. On the other hand, if the group engagement partner determined that the breach cannot be satisfactorily addressed, consistent with ISA 600 (Revised) the IESBA proposed to recognize that the GAF cannot use the CAF's work.

Comments

140. Some respondents, mainly regulatory respondents, were concerned that the differentiation in the process to address the consequences of a breach between CAFs within and outside the GAF's network was not appropriate and could have unintended consequences. They argued that the provision with respect to addressing a breach at a CAF within the GAF's network (paragraph R405.14 in the ED) was less restrictive than the provision for addressing a breach at a CAF outside the GAF's network (paragraph R405.15 in the ED). The respondents held this view as the latter set out specific actions for the CAF outside the GAF's network as well as the group engagement partner's determination of whether to use the CAF's work for purposes of the group audit.

141. A few commenters were of the view that the proposals related to a breach of independence by a CAF may not be workable in some jurisdictions as laws and regulations may prohibit a CAF from communicating information about the breach to a GAF located overseas.

142. A few respondents, including a MG member, raised that allowing the CAF outside the GAF's network to perform remedial work on areas of the engagement that are affected by its own breach may not be appropriate. They suggested that the IESBA consider providing guidance on other actions the component audit client or the GAF could take instead to address the consequences of the breach. A MG member also suggested that the Code provide examples of the circumstances in which the group engagement partner may determine whether additional actions are required and what those could be.

143. A respondent commented that a CAF should communicate the breach in writing to the GAF. Regarding the group engagement partner's actions upon the receipt of the CAF's communication, it was suggested that the group engagement partner should not be required to assess the CAF's objectivity but instead only review the CAF's assessment of the impact of the breach on that firm's objectivity.

IESBA Decisions

144. In light of the comments received, the IESBA considered that the purpose of the proposed guidance related to a breach of independence at a CAF is to assist the CAF in addressing the breach and, ultimately, to enable the GAF to make a determination as to whether it would be able to use the CAF's work. The focus of the CAF's and the GAF's assessments is to determine the significance and the impact of the breach on the CAF's objectivity and not to reassess or review the GAF's objectivity or ability to issue the group audit report. The IESBA determined to make amendments to the introductory paragraphs of this subsection to clarify this point. (See paragraphs 405.22 A1 and A2.)

145. Given this purpose, the IESBA agreed that there should be no difference in the provisions to address breaches identified by a CAF within or outside the GAF's network, as the objective of the guidance is the same. Section 405 therefore now includes actions that are relevant and appropriate for all CAFs (see paragraphs R405.23 and 405.23 A1). However, the IESBA noted that in the case of a breach at

a CAF within the GAF's network, the GAF also needs to apply paragraphs R400.80 to R400.89 in relation to the group audit, as applicable (see paragraph 405.22 A2).

146. Responding to the comments raising potential confidentiality issues related to the communication of the CAF's breach, the IESBA noted that ISA 600 (Revised)[46] requires that in establishing the overall group audit strategy and group audit plan, the group engagement partner evaluate whether the group auditor will be able to be sufficiently and appropriately involved in the work of the component auditor. The relevant application material[47] specifies that in evaluating whether the group auditor will be able to be sufficiently and appropriately involved in the work of the component auditor, the group auditor may obtain an understanding of whether the component auditor is subject to any restrictions that limit communication with the group auditor, including with regard to sharing audit documentation with the group auditor. Because of this upfront requirement in ISA 600 (Revised) in the context of establishing the group audit strategy and group audit plan, the IESBA does not believe that confidentiality issues regarding a CAF's communication on a breach to the GAF should cause any difficulty in practice.

147. Regarding the concerns about allowing the CAF to perform remedial actions, the IESBA believes that it is appropriate to allow a CAF to take actions to satisfactorily address the consequences of a breach. The IESBA noted that this approach is in line with the extant Code's provisions relevant to breaches of independence requirements by a firm. Nevertheless, the IESBA agreed to add application material, in line with the extant Code's provisions, to assist a CAF in considering any actions that might be taken to address the breach. (See paragraph 405.23 A1.)

148. In addition, Section 405 would require the group engagement partner to review any actions proposed or taken by a CAF to address the consequences of the breach (see paragraph R405.24(a)). If the group engagement partner determines that the breach has been satisfactorily addressed by the CAF and does not compromise the CAF's objectivity, the GAF may continue to use the work of the CAF 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 CAF's work. As the group engagement partner's determination will depend on the specific facts and circumstances, the IESBA did not believe that it would be appropriate for the Code to provide specific examples of the circumstances in which the group engagement partner may determine that such additional actions are required. (See paragraphs R405.25 and 405.25 A1.)

149. The IESBA discussed whether there was a compelling reason to be specific about the method of communication between the CAF and the group engagement partner and, specifically, whether to require written communication. The IESBA considered whether, similar to the approach to other requirements on communication in the Code, Section 405 should be principles-based regarding the method of communication. However, the IESBA also considered that the communication between the CAF and the group engagement partner forms a basis of subsequent reviews and discussions internally, and with TCWG of the group audit client. Therefore, the IESBA determined that, in this case, there were strong arguments to require written communication. (See paragraph R405.23(d).)

150. Regarding the group engagement partner's actions upon receipt of the CAF's communication, the IESBA agreed with the comments arguing that the group engagement partner cannot evaluate the impact of the breach on the CAF's objectivity. Based on the available information, the group engagement partner would only be able to review the CAF's assessment of the significance of the

[46] Paragraph 23 of ISA 600 (Revised)

[47] Paragraph A57 of ISA 600 (Revised)

breach and its impact on the CAF's objectivity. The IESBA therefore determined to make a few amendments to clarify this approach. (See paragraph R405.24(a) and (b).)

Communication of Breaches to TCWG of the Group Audit Client

151. Consistent with the provisions dealing with breaches in the extant Code, the IESBA believed it is necessary to involve TCWG of the group audit client in the process of addressing the consequences of a breach at a CAF.

152. In line with the extant Code's approach, the IESBA also proposed in the ED that the Code prohibit the GAF from using the work of the CAF for purposes of the group audit if TCWG of the group audit client do not concur with the GAF's assessment that action can be or has been taken to satisfactorily address the consequences of the breach.

Comments

153. Some respondents commented that it was not clear why the proposed requirement for the GAF to communicate breaches by a CAF outside the GAF's network was not the same as the provisions applicable for other breaches in extant paragraph R400.84 of the Code (i.e., discussion versus written communication as per extant paragraph R400.84).

154. Regarding the information communicated by the GAF on breaches by a CAF, a respondent suggested that the Code clarify that the group engagement partner's communication should focus on "the component auditor firm's assessment of" the significance of the breach and not the engagement partner's evaluation. In addition, it was suggested that the discussion with TCWG on the breach at a CAF include whether the GAF may use the work of the CAF or whether it will use other means to obtain the necessary audit evidence on the component audit client's financial information.

IESBA Decisions

155. Although the objective of the process that the CAF should follow when it identifies a breach of independence requirements is the same irrespective of whether the CAF is within or outside the GAF's network, the IESBA clarified that the objective of the communication of the breach to the TCWG of the group audit client is different. Therefore, the information communicated to TCWG would differ depending on whether the breach occurred at a CAF within or outside the GAF's network.

156. In the case of a breach at a CAF within the GAF's network, in line with the extant Code's provisions, the communication to TCWG should also include information about the policies and procedures of the GAF's network since those are relevant to the TCWG's considerations regarding the GAF's independence. (See paragraph 405.26 A1.)

157. However, if a breach has occurred at a CAF outside the GAF's network, the system of quality management addressing breaches at the CAF will be different compared with that within the GAF's network. Therefore, in the case of a breach at a CAF outside the GAF's network, the IESBA reaffirmed that the discussion with TCWG of the group audit client should focus on the actions that can be or has been taken to satisfactorily address the consequences of the breach, or whether the GAF will use other means to obtain the necessary audit evidence on the component audit client's financial information. (See paragraph R405.27.)

158. Regarding the method of communication, the IESBA discussed whether it would be necessary to require written communication of the breaches to TCWG in the case of breaches that occurred at

CAFs outside the GAF's network. Considering the comments provided by respondents and other stakeholders, the IESBA agreed to mirror the extant Code's approach in paragraphs R400.82 to R400.84. Accordingly, Section 405 requires the GAF to *discuss* with TCWG of the group audit client:

- The CAF's assessment of the significance and impact of the breach on the CAF's objectivity, including the nature and duration of the breach, and the action that can be or has been taken; and
- Whether:
    - The action will satisfactorily address, or has addressed, the consequences of the breach; or
    - The GAF will use other means to obtain the necessary audit evidence on the component audit client's financial information.

The IESBA determined that the GAF should communicate the information discussed above in writing and obtain the concurrence of TCWG of the group audit client that the action can be, or has been, taken to satisfactorily address the consequence of the breach. (See paragraphs R405.27 and R405.28.)

159. If TCWG do not concur that the action would satisfactorily address the consequences of the breach at the CAF, the GAF cannot use the work of the CAF for the purposes of the group audit and must use other means to obtain the necessary audit evidence on the component audit client's financial information. (See paragraph R405.29.)

V. Other Matters

Period During Which Independence is Required

160. A respondent to the ED raised that it was not evident from the ED how a CAF outside the GAF's network should apply the requirement in paragraph R400.30 of the Code (dealing with the period during which independence is required to be maintained) with respect to a group audit client. The respondent queried whether the CAF is required to be independent in accordance with the relevant ethical requirements that apply to the group audit until it issues its report to the GAF or by reference to another date, such as when the GAF issues its report. The commenter pointed out some practical challenges, such as knowledge about the relevant dates (the group audit report will be issued at some point in the following financial statement period), or in those scenarios where the CAF is not aware of whether it will be asked to remain as the CAF in a subsequent period (i.e., whether there is to be an on-going relationship).

161. The IESBA agreed that Section 405 should clarify the period during which independence is required of a CAF outside the GAF's network. As a general principle, the IESBA believes that a CAF outside the GAF's network should be independent during both the engagement period and the period covered by the group financial statements. In the context of a group audit, reflecting the guidance in paragraph 400.30 A1, the IESBA determined that the engagement period starts when the group audit team begins to perform the audit work and ends when the group audit report is issued. (See paragraph 405.14 A1.)

Changes in Component Auditor Firms and Components

162. The IESBA also noted that in practice, there might be circumstances in which the GAF requests another firm to perform audit work as a CAF 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 proposed guidance in the ED 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.

163. Leveraging guidance in the extant Code, the proposed guidance also addressed the situation where a NAS was provided by the CAF to the component audit client during or after the period covered by the group financial statements, but before the CAF begins to perform the audit work for the purposes of the group audit, and the NAS would not be permitted during the engagement period.

164. Respondents generally supported the proposed application material relating to changes in CAFs during or after the period covered by the group financial statements. However, commenters raised a few more scenarios for the IESBA's consideration that they felt the Code should also explicitly address.

165. It was also pointed out that there may be a situation where the GAF determines – after the period during which independence is required has commenced – that audit procedures are required to be performed at a component that is not a related entity. It was argued that the proposal did not include any mechanism for addressing a situation when an entity that is not a related entity is scoped in as a component (because it is subject to audit work) and therefore included in the definition of a group audit client.

166. The IESBA agreed with the suggestions to address further scenarios related to changes in CAFs or changes in the group audit client's circumstances. Accordingly, Section 405 provides more guidance regarding how to apply the provisions in Section 400 in the context of a group audit when:

- A firm has provided a NAS to a component audit client prior to the period covered by the group financial statements. (See paragraph 405.20 A3.)
- A firm has provided a NAS to a component audit client prior to becoming a CAF in the group audit of a PIE group audit client. (See paragraph 405.21 A1.)
- The group audit client later becomes a PIE. (See paragraph 405.21 A2.)

167. The IESBA also agreed to address the situation where an entity later becomes a component in the group audit. In this situation, Section 405 requires the GAF to apply the same process as the process set out in the extant Code addressing circumstances where an entity becomes a related entity because of a merger or acquisition. (See paragraph R405.19.)

VI. Effective Date

168. The main objective of the proposed changes to the Code relating to group audits was to articulate the specific independence provisions that form part of the concept of "relevant ethical requirements, including those related to independence" referred to in ISA 600 (Revised). The IESBA therefore proposed in the ED that the effective date of the proposed changes arising from this project should be aligned with the effective date of ISA 600 (Revised), i.e., effective for audits of financial statements for periods beginning on or after December 15, 2023.

169. Respondents to the ED generally supported the IESBA's proposal regarding the alignment of the effective date with ISA 600 (Revised). However, during the IESBA's outreach activities, a few stakeholders raised concerns regarding the proposed effective date, highlighting that it would not provide sufficient time for adoption and implementation. They noted a risk that this could lead to inconsistent application.

170. Although the IESBA recognized the challenges arising from the short period for adoption and implementation, it noted that it is in the public interest for the provisions to become effective at the same time as ISA 600 (Revised), especially given that the revised definition of ET is integral to ISA 600 (Revised).

171. Consequently, the IESBA agreed that:

- The changes to Section 400 relating to the revision to the definition of ET, the new provisions in Section 405, and the changes to the Glossary relating to group audits should be effective for audits and reviews of financial statements and audits of group financial statements for periods beginning on or after December 15, 2023.
- The conforming and consequential amendments should be effective as of December 15, 2023.

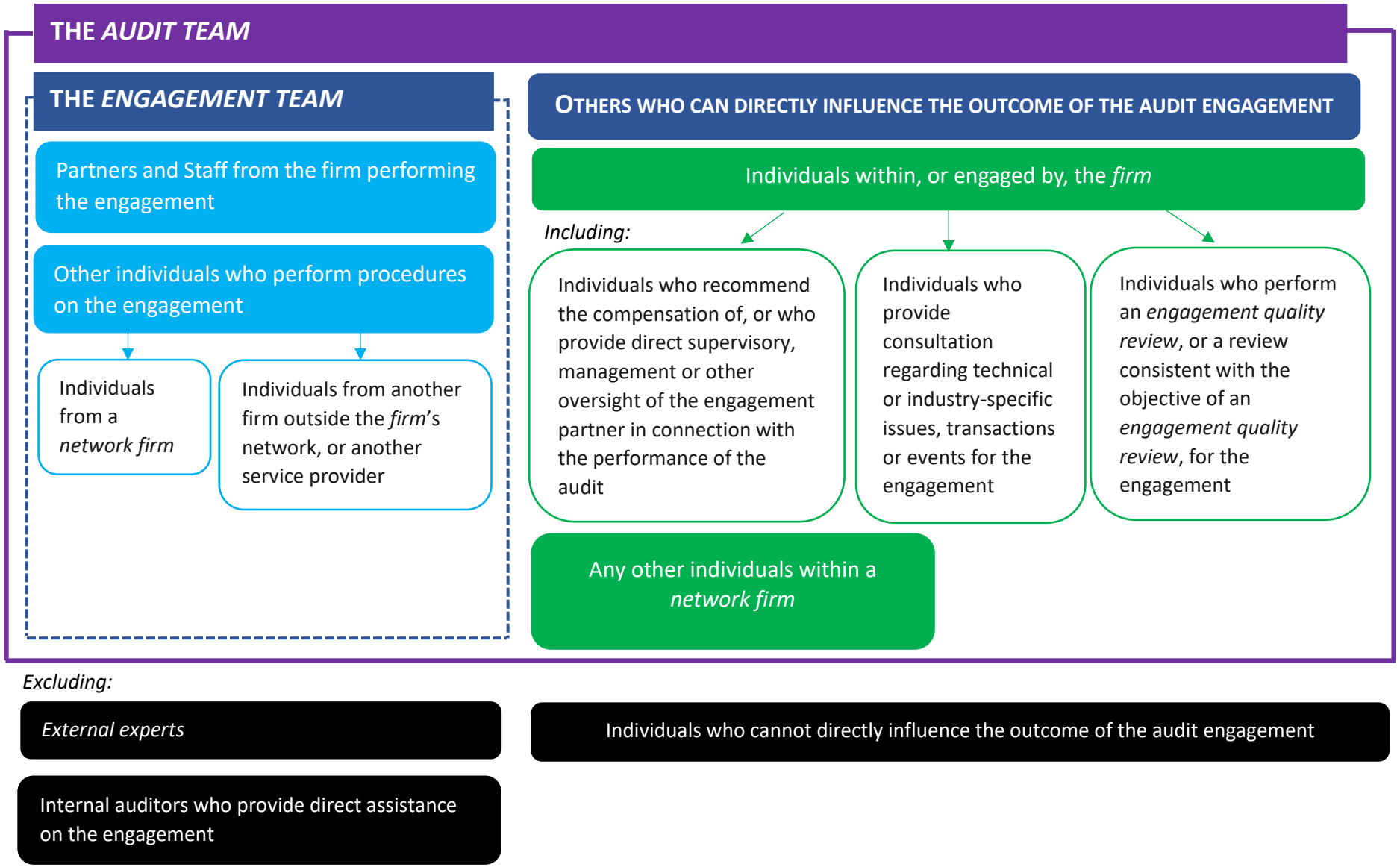
172. The IESBA also noted that the definitions of "audit client" and the "group audit client" make references to "listed entity," a term that has been replaced with the term "publicly traded entity" as part of the PIE project. As the changes from the PIE project will come into effect only a year later, in December 2024, the Glossary includes two different versions of these definitions with different effective dates.

173. The IESBA also determined to provide a transitional provision to address the case where a CAF outside the GAF's network has commenced an engagement to provide a NAS to a component audit client prior to the effective date of the revisions. Under this transitional provision, if a CAF outside the GAF's network has entered into an engagement to provide a NAS to a component audit client before December 15, 2023 and the work has already commenced, the CAF may continue the NAS engagement under the extant provisions of the Code until it is completed in accordance with the original engagement terms.

Appendix 1

Definitions of Engagement Team and Audit Team

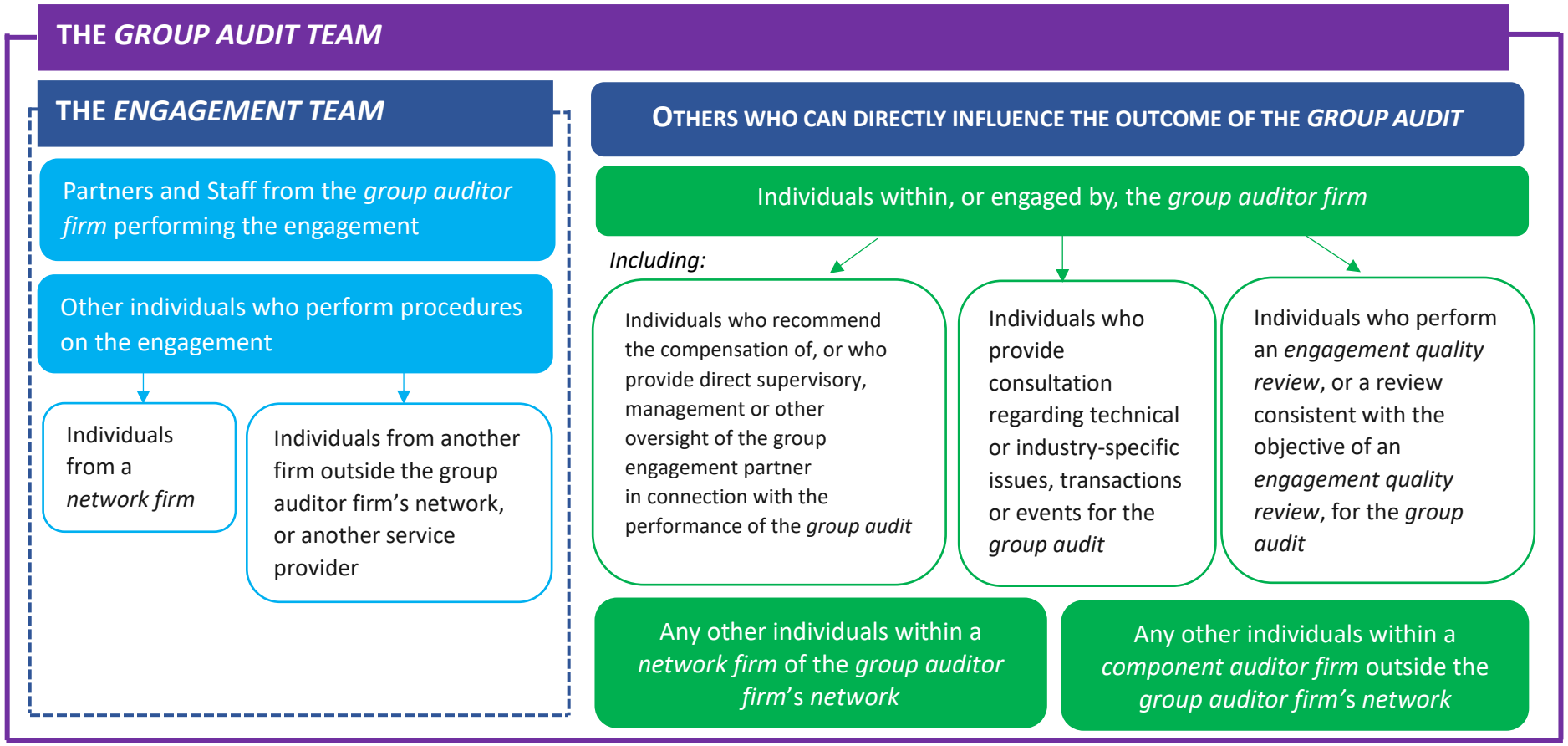
The diagram below sets out who is included in the engagement team and the audit team. Terms in italics are defined in the Glossary.



Appendix 2

Definitions of Engagement Team and Group Audit Team

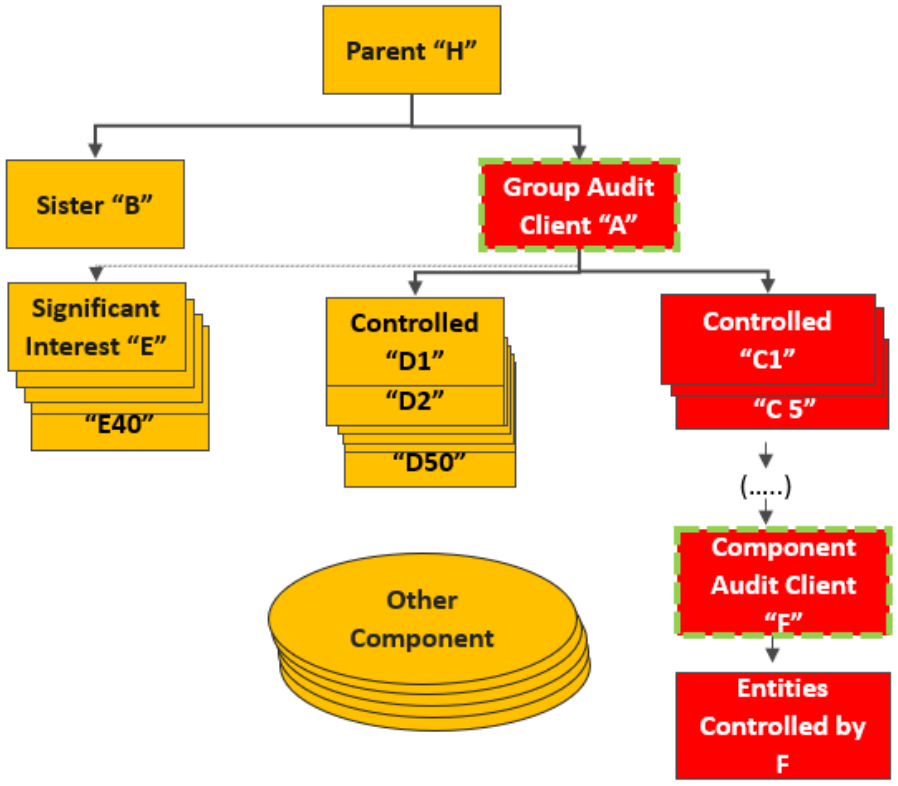
The diagram below sets out who is included in the engagement team and the group audit team. Terms in italics are defined in the Glossary.



Appendix 3

Approach to Independence for Audit Team Members outside the Group Auditor Firm's Network

For All Group Audit Clients



Independence in accordance with paragraph R405.6

Independence in accordance with paragraphs R405.7 to R405.8

The diagram is for illustrative purposes only. It does not seek to cover the full scope of all the potential related entities of the group audit client that might exist.

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