

RESPONSIBILITIES OF THE ENGAGEMENT PARTNER IN CIRCUMSTANCES WHEN THE ENGAGEMENT PARTNER IS NOT LOCATED WHERE THE MAJORITY OF THE AUDIT WORK IS PERFORMED

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As an initial response to concerns raised about situations when engagement partners are not located where the majority of the audit work is performed, including concerns raised by certain regulators and audit oversight bodies, this Staff Audit Practice Alert serves to remind auditors of the responsibilities of the engagement partner described in the ISAs.

ISA 600,¹ as revised and redrafted, was published in October 2007 and became effective for periods beginning on or after December 15, 2009. Feedback from regulators, audit oversight bodies, firms and [The Clarified ISAs—Findings from the Post-Implementation Review](#) indicates that there are issues with, and inconsistencies in, the application of ISA 600 to group audit engagements, as well as the application of the ISAs more broadly to audit engagements where other auditors are involved. These issues include: sufficiency of engagement partner involvement; the determination of component materiality; and the application of the ISAs when the engagement partner is at a different location from where the majority of the audit work is performed.

The IAASB's [Work Plan for 2015–2016](#) includes a focus on the topics of group audits and quality control. In particular, a variety of issues relating to group audits have been identified, including the issue of sufficient engagement partner involvement in an audit of group financial statements. The IAASB's Work Plan also includes a focus on the topic of quality control related to, among other areas, the responsibility of the engagement partner for the direction, supervision, performance and review of the audit engagement. Group audits and quality control have been identified as high priority projects relative to the Board's strategic objectives as set out in its [Strategy for 2015–2019](#), in particular with respect to ensuring that the ISAs "continue to form the basis for high-quality audits conducted worldwide, by responding on a timely basis to issues noted in practice and emerging developments." Further details on these efforts are described in the *Way Forward* section of this Alert.

Introduction

The manner in which an entity is structured typically has implications for how the audit is performed, including whether the audit is considered to be a group audit as defined in ISA 600.

Concerns have been expressed related to the performance of audits in circumstances when the engagement partner is not located where the majority of the audit work is performed. This circumstance arises, for example, when an entity is structured such that the entity is legally registered or maintains a correspondence address in one jurisdiction and the majority of the general and financial management, business activities and transaction processing are undertaken in a different jurisdiction.²

The structure of these entities may be driven by requirements of taxation or other laws and regulations, or may be designed for the purposes of being able to more effectively raise equity or debt capital. In some cases, there may be limited investments or operations in the entity's jurisdiction of legal registration, with the majority of management and business activities being undertaken in other jurisdictions.

In these circumstances, the engagement partner, or the group engagement partner and group engagement team where the entity is determined to be a group, may be located in the jurisdiction where the entity is legally registered or maintains a correspondence address, with the majority of the audit work being performed in the other jurisdiction(s) where general and financial management are located and where the business activities and related processing of transactions take place.

Because the engagement partner is not physically located where the audit work is being performed, accomplishing the objectives of the ISAs in these circumstances can pose different challenges than in situations when the engagement partner is located where the majority of the audit work is being performed.

In particular, concerns have been raised about how the engagement partner has taken responsibility for the direction, supervision, performance and review of the work, the adequacy of the audit documentation and whether, and how, the engagement partner has become satisfied that sufficient appropriate audit evidence has been obtained to enable the engagement partner to take responsibility for the auditor's report in these circumstances.

Those raising these concerns include certain regulators and audit oversight bodies. For example, these concerns are addressed in the UK Financial Reporting Council's [*Audit Quality Inspection's Annual Report 2013/2014*](#), the Netherlands Authority for Financial Markets [*Results of the inspection of the quality of statutory audits at the Big 4 audit firms, 25 September 2014*](#), and the Swiss [*Federal Audit Oversight Authority Activity Report 2014*](#).

Key Messages

The responsibilities of the engagement partner as set out in the ISAs apply to all audits, including in circumstances when the engagement partner is not located where the majority of the audit work is performed. This Staff Audit Practice Alert is intended to remind practitioners of the responsibilities of the engagement partner in those circumstances by focusing on certain requirements in the ISAs.

When auditing entities of all different structures, the focus of the engagement team,³ including the engagement partner,⁴ is the performance of a quality audit in accordance with ISAs that supports the auditor's conclusion that sufficient appropriate audit evidence has been obtained on which to base the auditor's opinion. How the ISAs (in particular, ISA 220, ISA 230⁵ and, when applicable, ISA 600) are applied to each audit engagement may vary based on the individual facts and circumstances due to the different structures of the entities whose financial statements are being audited.

- ISA 220 applies to all audit engagements that are conducted in accordance with ISAs, and ISQC 1⁶ applies to all firms conducting these engagements.
- For audits of group financial statements, ISA 600 indicates that the group engagement partner applies the requirements of ISA 220 regardless of whether the group engagement team⁷ or a component auditor performs the work on the financial information of a component.⁸ ISA 220 requires that the engagement partner take responsibility for the direction, supervision, performance and review of the group audit engagement and for being satisfied that sufficient appropriate audit evidence has been obtained on which to base the auditor's opinion on the financial statements.⁹
- ISA 600 assists the group engagement partner in meeting the requirements of ISA 220 when component auditors perform work on the financial information of components.¹⁰ ISA 600 requires that the group engagement team, including the engagement partner, evaluates whether sufficient appropriate audit evidence has been obtained on which to base the group audit opinion.¹¹
- The auditor may find ISA 600, adapted as necessary in the circumstances, useful when the auditor involves other auditors in the audit of financial statements that are not group financial statements.¹² In such cases, ISA 220 also applies.
- Appropriate documentation provides evidence of:
 - The direction, supervision, performance and review of the engagement by the engagement partner as required by ISA 220.
 - The involvement of the group engagement partner, as required by ISA 600 (for audits of group financial statements).
 - The basis for the conclusion that sufficient appropriate audit evidence has been obtained on which to base the auditor's opinion.

Applicability of the ISAs

Quality Control

ISA 220 establishes requirements for the engagement partner that are designed to facilitate a quality audit, including, among others, requirements for:

The requirements in ISA 220 apply to all engagements that are conducted in accordance with the ISAs, including audits of the financial statements of entities where the majority of the general and financial management of the entity and the majority of the business activities and related processing of transactions is located or undertaken in jurisdictions other than where the entity is registered or maintains a correspondence

- Taking responsibility for the overall quality on each audit engagement to which that engagement partner is assigned.¹³
 - Being satisfied that appropriate procedures regarding the acceptance and continuance of client relationships have been followed and determining that conclusions reached in this regard are appropriate.¹⁴
 - Taking responsibility for (i) the direction, supervision and performance of the audit engagement in compliance with professional standards and applicable legal and regulatory requirements; and (ii) the auditor’s report being appropriate in the circumstances.¹⁵
 - Taking responsibility for reviews being performed in accordance with the firm’s review policies and procedures.¹⁶
- Being satisfied, through a review of the audit documentation and discussion with the engagement team, that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued.¹⁷

Group Audits

ISA 600 deals with special considerations that apply to group audits, in particular those that involve component auditors.¹⁸ ISA 600 notes that a group will always have more than one component and provides guidance in identifying those components, including examples of various types of entity structures that may constitute a group.¹⁹ When an engagement is a group audit as defined in ISA 600, the requirements in that ISA apply.

ISA 600 explains that the group engagement partner is responsible for the direction, supervision and performance of the group audit engagement in compliance with professional standards and applicable legal and regulatory requirements, and whether the auditor’s report that is issued is appropriate in the circumstances.²⁰

ISA 600 assists the group engagement partner in meeting the requirements of ISA 220 in the context of a group audit.

ISA 600 also notes that, although component auditors may perform work on the financial information of the components for the group audit and as such are responsible for their overall findings, conclusions or opinions, the group engagement partner or the group engagement partner’s firm is responsible for the group audit opinion.²¹

Audits, Other than Group Audits, Involving Other Auditors

In an audit of financial statements that are not group financial statements, but where other auditors are involved in the audit, ISA 600, adapted as necessary in the circumstances, may be useful to the auditor, in planning and performing the audit in accordance with the requirements of the ISAs,²² including meeting the requirements of ISA 220.

Documentation

ISA 230 requires that audit documentation be prepared that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand:

- (a) The nature, timing and extent of the audit procedures performed to comply with the ISAs and applicable legal and regulatory requirements, with specific elements required to be documented;
- (b) The results of the audit procedures performed, and the audit evidence obtained; and
- (c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.²³

Audit documentation provides evidence that the audit complies with the ISAs,²⁴ including that the engagement partner and, as applicable, the group engagement partner, has taken responsibility for the direction, supervision, performance and review of the engagement as required by ISA 220.

ISA 600 includes specific documentation requirements for group audits,²⁵ including documentation of an analysis of components and the type of work performed on the financial information of the components; the nature, timing and extent of the group engagement team's involvement in the work performed by the component auditors; and written communications between the group engagement team and the component auditors about the group engagement team's requirements. These documentation requirements may also be useful in the audit of financial statements of an entity that is not a group, but in which other auditors are involved.

Way Forward

The IAASB will continue to seek further feedback on issues identified by regulators and audit oversight bodies during their inspections and about areas where auditors find it challenging to apply the ISAs, including further information about the circumstances addressed in this Staff Audit Practice Alert, to inform its work on group audits and quality control. In particular, within the project on quality control, the IAASB will also explore how the engagement partner's responsibilities are articulated within the ISAs and whether these responsibilities may need clarification.

A Discussion Paper is planned for December 2015 to explore more holistically what actions the IAASB and others could take to enhance audit quality, including identification of potential areas for improvement within the ISAs and areas where more practical guidance may be needed to assist auditors in applying the ISAs as the global business environment continues to evolve. Feedback from this consultation will be used to determine the scope of standard-setting projects, including informing the basis for changes to the ISAs or additional guidance that may be necessary.

For more information on these projects, visit the IAASB's website at <http://www.iaasb.org/projects/group-audits-isa-600> and <http://www.iaasb.org/projects/quality-control>.

Endnotes

1. ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*
2. These entities have been referred to by some as “letterbox companies”.
3. Paragraph 7(d) of ISA 220, *Quality Control for an Audit of Financial Statements*, defines the engagement team as “all partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform audit procedures on the engagement. This excludes an auditor’s external expert engaged by the firm or a network firm. The term “engagement team also excludes individuals within the client’s internal audit function who provide direct assistance on an audit engagement when the external auditor complies with the requirements of ISA 610 (Revised 2013), *Using the Work of Internal Auditors*.”
4. Paragraph 7(a) of ISA 220 defines the engagement partner as “the partner or other person in the firm who is responsible for the audit engagement and its performance, and for the auditor’s report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.”
5. ISA 230, *Audit Documentation*
6. 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*
7. Paragraph 9(i) of ISA 600 defines the group engagement team as “partners, including the group engagement partner, and staff who establish the overall group audit strategy, communicate with component auditors, perform work on the consolidation process, and evaluate the conclusions drawn from the audit evidence as the basis for forming an opinion on the group financial statements.”
8. ISA 600, paragraph 5
9. ISA 220, paragraphs 15–16
10. ISA 600, paragraph 5
11. ISA 600, paragraph 44
12. ISA 600, paragraph 2
13. ISA 220, paragraph 8
14. ISA 220, paragraph 12
15. ISA 220, paragraph 15
16. ISA 220, paragraph 16
17. ISA 220, paragraph 17
18. ISA 600, paragraph 1
19. ISA 600, paragraph A2
20. ISA 600, paragraph 11
21. ISA 600, paragraph 44
22. ISA 600, paragraph 2
23. ISA 230, paragraph 8
24. ISA 230, paragraph A7
25. ISA 600, paragraph 50

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The objective of the IAASB is to serve the public interest by setting high-quality auditing, assurance, and other related standards and by facilitating the convergence of international and national auditing and assurance standards, thereby enhancing the quality and consistency of practice throughout the world and strengthening public confidence in the global auditing and assurance profession.

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