We will continue with:

1. **Applying the Conceptual Framework**

   In this KLiP, we will cover the sub-topic

   Threat to independence arising from client Mergers and Acquisitions

   An entity might become a related entity of an audit client because of a merger or acquisition. A threat to independence might be created due to interests or relationships between a firm or network firm and the related entity.

   The Code sets out how to address these threats, if it arises:

   - ✓ The firm shall identify and evaluate the interests and relationships with the related entity that, taking into account any actions taken to address the threat, might affect its independence and therefore its ability to continue the audit engagement after the effective date of the merger or acquisition; and

   - ✓ The firm shall take steps to end any interests or relationships that are not permitted by the Code by the effective date of the merger or acquisition.

   It might not always be reasonably possible to end an interest or relationship creating a threat by the effective date of the merger or acquisition. This might be because the firm provides a non-assurance service to the related entity, which the entity is not able to transit in an orderly manner to another provider by that date. In such exceptional situations, the firm shall:

   - ➢ Evaluate the threat that is created; and

   - ➢ Discuss with TCWG the reasons as to why the interest or relationship cannot reasonably be ended by the effective date and the evaluation of the level of the threat.

   Following the discussion with TCWG, if the firm is requested to continue as the auditor, the firm shall do so, only if the following conditions are fulfilled:

   - ✓ The interest or relationship will be ended as soon as reasonably possible but no later than six months after the effective date of the merger or acquisition;

   - ✓ Any individual who has such an interest or relationship, including the one that has arisen through performing a non-assurance service and the engagement for quality control review will not be a member of the engagement team for the audit; and

   - ✓ Transitional measures will be applied, as necessary, and discussed with TCWG.

Examples of transitional measures include:

1. Having a professional accountant review the audit or non-assurance work, as appropriate.

2. Having a professional accountant, who is not a member of the firm to express opinion on the financial statements by performing a review that is equivalent to an engagement quality control review.

3. Engaging another firm to evaluate the results of non-assurance service or re-perform them so that the other firm takes responsibilities for the services.

In some cases, the firm might have also completed a significant amount of work on the audit, prior to the effective date of the merger or acquisition, and might be able to complete the remaining within a short period of time. In such cases, if TCWG requests the firm to complete the audit while the client continue mergers or acquisition, then, the firm shall only do so if it:

i. Has evaluated the level of the threat and discussed the results with TCWG;

ii. Complies with the requirements of TCWG, as stated above;

iii. Ceases to be the auditor no later than the date that the audit report is issued.

Even after all the above requirements are met, if the firm determines that the threat cannot be addressed, such that the objectivity would be compromised, then the firm shall cease to be the auditor.

Documentation:

The firm shall document:

a. Any interests or relationships identified, that will not be ended by the effective date of the merger or acquisition and the reasons as to why they will not be ended;

b. The transitional measures applied;

c. The results of the discussion with TCWG; and

d. The reasons why the previous and current interests and relationships do not create a threat such that the objectivity would be compromised.

With this we come to the end of the KLiP. We continue the discussion about breach of independence, in our next KLiP.

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