ISA 600 – Audits of Group Financial Statements

Len Jui, Board member and ISA 600 Task Force Chair

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Task Force Members and Staff

• Task Force members
  – Len Jui, Task Force Chair (supported by Susan Jones)
  – Robert Dohrer
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  – Wolf Böhm
  – Josephine Jackson
  – Dora Burzenski (Correspondent member)

• Staff
  – Jasper van den Hout
  – Dan Montgomery
Section I: Public Interest Issues
<table>
<thead>
<tr>
<th>KEY PUBLIC INTEREST ISSUES</th>
<th>DESCRIPTION OF ISSUE(S) TO BE ADDRESSED</th>
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</thead>
</table>
| Keeping the IAASB’s Standard on Group Audits Fit for Purpose | • Scope of the Standard  
• Linkages with Other Standards  
• Adaptability and Scalability |
| Encouraging Proactive Management of Quality at the Engagement Level | • Managing and Achieving Quality in a Group Audit  
• Planning and Performing a Group Audit Engagement  
• Robust Communications and Interactions Between the Group Engagement Team / Group Engagement Partner and Component Auditors  
• Fostering the Appropriate Exercise of Professional Skepticism  
• Access to People and Information  
• Component Materiality |
The IAASB is asked for its views on the identified key public interest issues as set out in Section I of Agenda Item 6.
Section II: Risk-Based Approach
Focus of Extant ISA 600

Significant Component A
Significant Component B
Non-significant Component C
Non-significant Component D
Group FS

Assets
Liabilities
Equity
Revenue
Costs/Expenses
Main Features of the Risk-Based Approach

- Focuses on identifying, assessing and responding to the risks of material misstatement (RoMM) of the group financial statements
  
  “The right work done by the right people at the right locations”

- Think about
  
  - **What** *(identifying and assessing RoMM)*
  
  - **How** and **when** *(developing the strategy to respond to assessed risks)*
  
  - By **whom** and **where** *(determining which resources will perform procedures to obtain evidence)*

- Greater alignment with the requirements in ISA 315 (Revised) and ISA 330

- Greater focus on the group engagement team’s responsibility, with the assistance of component auditors as needed
Risk-Based Approach

Assets

Liabilities

Equity

Revenue

Costs/Expenses

Component A
Component B
Component C
Component D

Group FS
Similarities between Extant and Risk-Based Approach

• Obtain sufficient appropriate audit evidence to provide a basis for the opinion on the group financial statements

• Understanding the entity and its environment, including the group structure, business activities, and internal control

• Involvement of component auditors, as appropriate, in
  – Risk assessment procedures (understanding the entity and its environment and system of internal control)
  – Identification and assessment of risks of material misstatement
  – Responses to the assessed risks of material misstatement

• Responsibilities of the group engagement partner
Considerations in Applying the Risk-Based Approach

- Few to Many
- Single line of business in same industry vs. Different lines of business in different industries
- Nature of business/operations: Common or centralized vs. Unique, de-centralized
- System of internal control, including information system
- None or lower vs. Greater likelihood of involvement of component auditors
Risk-Based Approach – Scenario 1

Risk-based approach considerations

- Single location
- One line of business
- Single non-complex information system

Applying the risk-based approach

- ISA 600 does not apply
- Identify, assess and respond to RoMM at the assertion level by applying ISA 315 (Revised) and ISA 330
- Direction, supervision and review in accordance with ISA 220 (Revised)
Risk-Based Approach – Scenario 2

Risk-based approach considerations

- Entity A is a holding company with no business activities
  - Business Unit 1 = 75% of the group, Business Unit 2 = 25%
  - Both locations in same line of business, single non-complex information system

Applying the risk-based approach

- ISA 600 applies (special considerations in applying requirements in ISA 315 (Revised), ISA 330 and ISA 220)
- Approach to obtaining audit evidence
  - Focus on significant accounts/ CoT/ disclosures
  - Consolidation: Identify, assess and respond to RoMM arising from consolidation process
- Group engagement team is able to do the work itself
  - Ability to perform some testing centrally
  - Sufficient resources available to obtain evidence from both BUs as needed
Risk-Based Approach – Scenario 2 (Continued)

- Assets: Audited by GET
- Liabilities: Audited by GET
- Equity: Audited by GET
- Revenue: Audited by GET
- Costs/Expenses: Audited by GET
Risk-Based Approach – Scenario 3

Entity A

BU 1

BU 2

Risk-based approach considerations
• Same as Scenario 2

Applying the risk-based approach
• Same as Scenario 2 but group engagement team is not able to do the work itself
  o Component auditor will perform procedures at BU 2
  o Requirements in ISA 600 apply related to communication with and involvement in the work of component auditors
Risk-Based Approach – Scenario 3 (Continued)

<table>
<thead>
<tr>
<th>Category</th>
<th>Business Unit 1</th>
<th>Business Unit 2</th>
<th>Group FS</th>
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</thead>
<tbody>
<tr>
<td>Assets</td>
<td>Audited by GET</td>
<td>Audited by CA</td>
<td></td>
</tr>
<tr>
<td>Liabilities</td>
<td>Audited by GET</td>
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<td>Costs/ Expenses</td>
<td>Audited by GET</td>
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</tr>
</tbody>
</table>
Risk-Based Approach – Scenario 4

Risk-based approach considerations

- Entity A is a holding company with no activities
  - BU 1 = 40% of the group, BU 2 = 40%, BU 3 = 10% and BU 4 = 10%
  - Multiple geographic locations, several lines of business, different information systems

Applying the risk-based approach

- Greater complexity due to more locations and different lines of business, so more focus on:
  - Understanding the system of internal control, including the information system and commonality of controls across BUs
    - Assume BU 1, 2 and 3 use a different system than BU 4
  - Involvement of component auditors
    - Component auditors will perform work on BU 2 and 4 based on instructions from the group engagement team
    - Requirements in ISA 600 apply related to communication with and involvement in the work of component auditors, and may be more complex because group has multiple geographical locations (cultural differences, different ethical standards, etc.).
Risk-Based Approach – Scenario 4 (Continued)

- **Business Unit 1**: Audited by GET
- **Business Unit 2**: Audited by CA 1
- **Business Unit 3**: Audited by CA 2
- **Business Unit 4**: Audited by GET

- **Assets**
  - Group FS: Audited by GET
  - Business Unit 1: Audited by GET
  - Business Unit 2: Audited by CA 1
  - Business Unit 3: Audited by CA 2
  - Business Unit 4: Audited by GET

- **Liabilities**
  - Group FS: Audited by GET
  - Business Unit 1: Audited by GET
  - Business Unit 2: Audited by CA 1
  - Business Unit 3: Audited by GET

- **Equity**
  - Group FS: Audited by GET
  - Business Unit 1: Audited by GET

- **Revenue**
  - Group FS: Audited by GET
  - Business Unit 1: Audited by GET
  - Business Unit 2: Audited by CA 1
  - Business Unit 3: Audited by GET
  - Business Unit 4: Audited by CA 2

- **Costs/Expenses**
  - Group FS: Audited by GET
  - Business Unit 1: Audited by GET
  - Business Unit 2: Audited by GET
  - Business Unit 3: Audited by GET
  - Business Unit 4: Audited by GET
Risk-Based Approach – Other Considerations

• Shared service centers
• Group with a large number of individually insignificant components
• Use of several IT systems
• Changes in management or key personnel at one or more locations
• Locations where uncorrected misstatements were identified in previous year
• Locations where internal control deficiencies were identified in previous year
The IAASB is asked for its views on

a) The description of the risk-based approach to planning and performing an audit of group financial statements, including the Task Force’s initial thoughts about significant components as discussed in paragraph 22

b) The indicative drafting as presented in Agenda Item 6-A
Section III: Special Considerations in an Audit of Group Financial Statements
Structure, Scope and Applicability of ISA 600 (Revised)

• Appendix 1 illustrates a possible structure for the revised standard
  – Stronger linkages to foundational standards, as discussed with Board in March 2019

• Scope and applicability
  – Linked to definition of group financial statements

• Task Force recognizes the importance of addressing the fundamental question of whether certain situations are “in or out” of scope of ISA 600
  – Use of shared service centers
  – Various multi-location scenarios, for example, an entity with multiple branches or an entity with several warehouse locations
  – Use of other auditors for inventory counts

• Task Force also has considered the PCAOB proposed standard on use of other auditors
Scope and Applicability – Matters for IAASB Consideration

The IAASB is asked for its views on

a) The proposed structure as set out in Appendix 1 of Agenda Item 6

b) The scope of the revised standard and the Task Force’s proposals in this regard
The IAASB is asked for its views on the proposed changes to the definitions of

a) Component
b) Group financial statements
c) Consolidation process
The IAASB is asked for its views on

a) The proposed changes to the engagement acceptance and continuance and planning considerations

b) The indicative drafting as presented in Agenda Item 6-B
Identifying and Responding to RoMM

• The following special considerations related to the risk-based approach were discussed by the Task Force
  – Group-wide controls
    • Over reliance on group-wide controls
  – Use of audit evidence from audits required by statute, regulation or for another reason
    • Involvement of the GET should be similar to any other situation in which work is performed on a component by a component auditor
  – Shared service centers
The IAASB is asked for its views on the other special considerations related to the performance of a group audit engagement
The IAASB is asked for its views on the matters in the sections on

a) Involvement of, and communications with, component auditors

b) Evaluating the work of component auditors and sufficiency and appropriateness of audit evidence obtained

c) Communication with group management and those charged with governance

d) Documentation
Section IV: Way Forward