

Group Audits – Matters for Consideration by the IAASB

Division of Responsibility

1. Division of responsibility was discussed at the May 2003 IAASB meeting, where some of the IAASB members were of the opinion that, although used in a limited number of countries (reference was made to the US, Brazil and Italy), it is a valid and acceptable concept that can be applied elsewhere in the world and, therefore should be given equal prominence in the proposed revised ISA 600 “Considering the Work of Other Auditors.” Other IAASB members were of the opinion that the proposed revised ISA 600 should provide for both alternatives, but clearly indicate sole responsibility as the preferred alternative. A minority of the IAASB members were of the opinion that the proposed revised ISA 600 should not provide for division of responsibility. The IAASB concluded that the proposed revised ISA 600 should provide for both alternatives, indicating that sole responsibility was the preferred alternative. The IAASB also requested the task force to expand the guidance provided on division of responsibility.
2. Division of responsibility was also discussed at the May 2003 CAG meeting, where the EC representative indicated a preference for the group auditor to take sole responsibility for the auditor’s report on the group financial statements. After debate, it was concluded that, should the IAASB agree to retain division of responsibility as an alternative, the explanatory memorandum accompanying the exposure draft should provide the conceptual reason(s) for retaining it.
3. Although not originally planned for discussion, IOSCO raised division of responsibility at a meeting of representatives of the IAASB and IOSCO Audit Working Party held on June 30, 2003. IOSCO indicated that they considered sole vs. division or responsibility as an important matter to be resolved by the IAASB, and was of the opinion that the IAASB should not provide for current practice, but for the best quality approach in the proposed revised ISA 600. IOSCO also indicated that it would be disappointed if the IAASB provided for both alternatives, and strongly urged the IAASB to decide on one approach. However, it was noted that should the IAASB agree to provide for both alternatives, sufficient guidance should be provided for both.
4. The task force reconsidered the matter at its June 24-25, 2003 meeting (which took place before the IOSCO meeting referred to above). The task force considered a memorandum received from Randy Noonan with regard to division of responsibility. The task force’s discussion included the following:
 - Whether a theoretical (conceptual) basis for division of responsibility existed. Division of responsibility is a long established practice in the US, which grew out of a practical need for cooperative effort by the accountancy profession. The task force could not identify a theoretical justification for the approach.
 - Whether the procedures performed by a group auditor, who takes sole responsibility for the auditor’s report on the group financial statements, are sufficient – i.e. to enable the group auditor to take sole responsibility. The task force agreed that the proposed revised ISA 600 and IAPS should continue to provide for the group auditor to obtain

- sufficient appropriate audit evidence on which to base the audit opinion on the group financial statements. This may include the group auditor getting involved in certain aspects of the other auditor's audit process.
- Whether one of the two alternatives is inherently more in the public interest? The task force agreed that this should be a feature of the consultations process, i.e. the matter should be discussed and relevant questions asked in the explanatory memorandum accompanying the exposure drafts.
 - The impact of a decision not to provide for division of responsibility on international convergence. The task force concluded that the proposed revised ISA 600 should provide for both alternatives, as the deletion of division of responsibility will have an impact on international convergence.
5. The majority of the task force members were of the opinion that the conclusion reached by the IAASB at the May 2003 meeting should be implemented by the task force. The task force agreed that:
- (a) The introduction to the proposed revised ISA should refer to both alternatives, indicating that sole responsibility is the preferred alternative, but that guidance on division of responsibility is provided in a separate section at the end of the ISA.
 - (b) The criteria for applying division of responsibility should be reconsidered.
 - (c) The IAPS will only apply in circumstances where the group auditor takes sole responsibility for the auditor's report on the group financial statements.

Does the IAASB agree with the conclusions reached by the task force?

INTRODUCTORY PARAGRAPH AND GUIDANCE IN A SEPARATE SECTION

6. The majority of the task force members propose the following wording to be included in the introduction to the proposed revised ISA:
- “The group auditor ordinarily takes sole responsibility for the audit opinion on the group financial statements and does not refer to the other auditor in the auditor's report on the group financial statements. While this practice is considered desirable, it is acknowledged that national practice in some jurisdictions permits the group auditor to refer to the other auditor in the auditor's report on the group financial statements. This is referred to as “division of responsibility.” Paragraphs ... to ... of this ISA apply when the auditor takes sole responsibility for the auditor's report on the group financial statements. Division of responsibility is dealt with in paragraphs ... to”
7. Earlier reference to “national regulation” (“local regulation” in the existing ISA 600) has been replaced with “national practice,” as in the US, for example, division of responsibility is provided for in national auditing standards and not in national regulation. (However, one could argue that the fact that the PCAOB has been established in accordance with legislation and regulation and has adopted the national auditing standards in accordance with powers entrusted to it by legislation and regulation gives “legal-backing” to those standards.)
8. Agenda Item 14-B contains a summary of national practices, which was prepared at the start of the project.

9. IOSCO has indicated that, should the IAASB agree to provide for both alternatives, sufficient guidance should be provided for both (i.e. it would be unacceptable to have fifty paragraphs on sole responsibility and five paragraphs on division of responsibility). However, as the group auditor's procedures in relation to the other auditor's work are limited where the group auditor divides the responsibility, the guidance, by definition, will be less than the guidance to be applied in circumstances where the group auditor takes sole responsibility.

Does the IAASB agree with the proposed wording to be included in the introduction to the proposed revised ISA 600 and the fact that more guidance on division of responsibility will not be included?

CRITERIA FOR APPLYING DIVISION OF RESPONSIBILITY

10. According to the US AU 543 "Part of Audit Performed by Other Independent Auditors" (which was distributed by Susan Jones at the May 2003 IAASB meeting), the group auditor may decide to divide responsibility under the following circumstances:

"In some situations, it may be impracticable for the principal auditor to review the other auditor's work or to use other procedures which in the judgment of the principal auditor would be necessary for him to satisfy himself as to the audit performed by the other auditor. Also, if the financial statements of a component audited by another auditor are material in relation to the total, the principal auditor may decide, regardless of any other considerations, to make reference in his report to the audit of the other auditor."

11. The proposed revised ISA 600 reviewed at the May 2003 IAASB meeting, contained the following paragraph relevant to sole responsibility only:

"In some circumstances there may be restrictions on the group auditor's access to component information, component management or the other auditor, for example when a subsidiary operates in a foreign jurisdiction or in the case of an associated company. **If this difficulty cannot be resolved through group management, the group auditor should consider the likely impact of this scope limitation on the auditor's report on the group financial statements.**"

12. The task force discussed whether it is appropriate for the same circumstance to lead to a scope limitation under the one approach (sole responsibility), and to be treated as a criteria to decide whether to follow the other approach (division of responsibility). The task force concluded that the group auditor should only be allowed to divide responsibility if it is impracticable to review the other auditor's work or to perform other procedures *and* the component's financial information is material in relation to the group financial statements. (That is, not *or* as per the US AU 543.)

Does the IAASB agree with the proposed criteria for dividing responsibility?

Approach to be Followed in the Proposed Revised ISA 600

13. A task force member noted that the existing ISA 600 (and proposed revised ISA 600 reviewed at the May 2003 IAASB meeting) follows a "bottom up" approach as opposed to a "top down" approach. These documents require that, when group financial statements include financial information of components that are audited by other auditors, the group auditor

should (i.e. has to) determine how the work of the other auditor will affect the audit of the group financial statements.

14. The task force believes that the decision as to whether to request an other auditor to perform work on a component's financial information is made later in the audit process, i.e. after the group auditor has conducted the group risk assessment, categorized the components based on the results of the group risk assessment and determined the scope of work to be performed on the components' financial information. The task force agreed that the proposed revised ISA 600 should be redrafted accordingly.

Does the IAASB agree with the proposed approach to be taken in the revised ISA 600?

Structure of the IAPS (as Stand-alone Document)

15. The task force reconsidered the proposed IAPS and agreed that the document should be restructured and that additional practical guidance should be provided. In addition, the IAPS should be a stand-alone document and, as a result, incorporate guidance on the basic principles and essential procedures contained in the proposed revised ISA 600.
16. The task force also requested IAASB staff to redraft the guidance on group-wide controls, the categorization of the components based on the group risk assessment, and the scope of work to be performed at components.
17. A small drafting group has prepared a revised proposed IAPS for consideration at the July 2003 task force meeting. The table in the appendix provides an indication of the structure of the revised proposed IAPS.

Does the IAASB have any comments on the above and on the table in the appendix?

Group Materiality

18. The task force reconsidered the proposed guidance on group materiality, and confirmed that the guidance was based on guidance received from firms at the start of the project. (That is, the proposed guidance incorporates the principles of firm guidance, but does not reflect the formulae-driven approaches.) The task force also acknowledged that the revision of ISA 320 "Group Materiality" will impact the proposed guidance. As a result, the task force agreed that the proposed guidance:
 - (a) Should be limited to that included in the proposed IAPS reviewed at the May 2003 IAASB meeting;
 - (b) Should not be included in a separate section, but in the section that deals with the scoping of work to be performed on the component's financial information; and
 - (c) Should be revised once the Audit Materiality Task Force has completed its project. (Consideration should be given to including group materiality in the proposed revised ISA 320.)

Does the IAASB have any comments on the above?

Appendix

Introduction

Purpose and Overview of IAPS
Application of IAPS
Responsibility
Definitions

Acceptance and Continuance as Group Auditor

Obtaining an Understanding of the Group and Its Components Sufficient to Determine Whether to Accept or Continue the Engagement
Determining Whether to Accept or Continue the Engagement

Terms of Engagement

Obtaining Audit Evidence in Relation to the Components' Financial Information

Assessing the Risks of Material Misstatement of the Group Financial Statements and Categorizing the Components
Extending the Understanding of the Group and Its Components Obtained to Determine Whether to Accept or Continue the Engagement
Group-wide Controls
Visits to Components
Group Risks Assessment
Categorizing the Components
Testing Group-wide Controls
Scoping the Work to be Performed on the Components' Financial Information
Other Auditors
The Other Auditor's Professional Qualifications, Independence, Professional Competence and Resources
The Other Auditor's Quality Control Process
Communication
The Other Auditor's Report
Reviewing the Other Auditor's Work
Considering the Other Auditor's Findings

Auditing the Consolidation Process

Obtaining an Understanding of the Consolidation Process
Assessing the Risks of Material Misstatement of the Group Financial Statements and Responding Thereto
Reporting Packages
Consolidation Adjustments
Components With Different Financial Year-ends

Management Representations

Evaluating the Sufficiency and Appropriateness of Audit Evidence Obtained

Going Concern

Subsequent Events

Communication With Group Management and Those Charged With Governance

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