



INTERNATIONAL FEDERATION OF ACCOUNTANTS

545 Fifth Avenue, 10th Floor
New York, New York 10017
Internet: <http://www.ifac.org>

Tel: +1 (212) 286-9344
Fax: +1 (212) 856-9420

Agenda Item 7

Committee: IAASB
Meeting Location: New York
Meeting Date: May 11-13, 2003

Group Audits

Objectives of Agenda Item

1. To review and approve an exposure draft of the proposed revised ISA 600 "Considering the Work of Other Auditors."
2. To review a proposed IAPS on The Audit of Group Financial Statements. (First read.)

Background and Activities Since Last IAASB Discussions

The IAASB reviewed a draft of the proposed revised ISA 600 in December 2002. The Group Audits Task Force considered the IAASB's comments and finalized the proposed revised ISA for approval as an exposure draft at this meeting. (Due to the significance of the changes, the IAASB is provided with a clean copy only.)

The Task Force also prepared a proposed IAPS on The Audit of Group Financial Statements.

Scope of Proposed Pronouncements

The proposed revised ISA 600 establishes basic principles and essential procedures and provides guidance when a group auditor considers the work of other auditors in an audit of group financial statements. The proposed IAPS provides guidance on the application of ISAs to the audit of group financial statements.

Although both pronouncements are written in the context of an audit of group financial statements, they indicate that the basic principles, essential procedures and guidance also apply:

- (a) To the audit of financial statements (prepared in accordance with an applicable financial reporting framework or other suitable criteria) that combine the financial information of components, i.e. where a parent does not exist.
- (b) When an auditor plans to use the work of another auditor in a context other than the audit of group financial statements, e.g. to obtain audit evidence in relation to inventory held at a remote location.

Definitions

The majority of the definitions are included in the proposed revised ISA 600. The proposed IAPS contains a reference to the definitions.

The existing ISA 600 defines "other auditor" as "an auditor, other than the principal auditor, with responsibility for reporting on the financial information of a component which is included in the

financial statements audited by the principal auditor. Other auditors include affiliated firms, whether using the same name or not, and correspondents, as well as unrelated auditors.”

The Task Force considered it necessary to clarify the term “other auditor” as follows: “Other auditor” means an auditor, other than the group auditor, reporting on financial information of a component, and includes an auditor from:

- (a) The group auditor’s office;
- (b) Other office of the group auditor’s firm, whether using the same name or not;
- (c) A network firm, whether using the same name or not;
- (d) A correspondent; and
- (e) An unrelated firm.

Reference to “other auditor” in the proposed pronouncements should be read with the above definition in mind.

Proposed Revised ISA 600 – Framework for Revision

The following essential procedures form the framework for the revision of ISA 600:

“The group auditor should consider whether the work of the other auditor is likely to provide sufficient appropriate audit evidence in relation to the component’s financial information. In determining the nature, timing and extent of the audit procedures to be performed in relation to the other auditor’s work and report, the group auditor should consider the following:

- (a) The group auditor’s evaluation of information obtained with regard to the professional qualifications, independence, professional competence and resources of the other auditor.
- (b) Where relevant, representation from the other auditor that the other auditor’s quality control process complies with the quality control standards of the International Federation of Accountants as they relate to the audit of financial statements.
- (c) Whether the component, individually or together with other components, may give rise to risks of material misstatement of the group financial statements.
- (d) Whether the auditor’s report on the group financial statements refers to a division of responsibility.”

An illustrative example of the application in practice of the above is set out below (the illustrative example applies to an environment where division of responsibility is not permitted):

	Other auditor from the group auditor's office, other office of the group auditor's firm or network firm	Other auditor from firm with good reputation / quality control process	Group auditor uncertain as to reputation / quality control process of other auditor
Component – low risk of material misstatement of group financial statements	Request closing memorandum on examination	Request closing memorandum Consider rotational visit	Request representation regarding quality control process Request closing memorandum on examination Visit on rotational basis
Component – high risk of material misstatement of group financial statements	Request closing memorandum on examination Attend closing meeting	Request closing memorandum on examination Review working papers Attend closing meeting	Request representation regarding quality control process Active involvement in planning Request closing memorandum on examination Review working papers Attend closing meeting

Proposed IAPS – Framework for Development

The proposed IAPS is based on the proposed Audit Risk Standards.

The Task Force prepared the attached framework to assist with the development of the IAPS. It is suggested that the IAASB reviews the proposed IAPS with reference to the framework. For example, paragraph 40 of the proposed IAPS provides guidance on the categorization of components, based on the group auditor's risk assessment.

Paragraph 43 notes that the group auditor considers the following in determining the scope of work to be performed at each component:

- (a) Assessment of risks of material misstatement of the group financial statements, and whether a component, individually or together with other components, may give rise to risks of material misstatement of the group financial statement.
- (b) Audit evidence obtained in evaluating the design and implementation of centralized internal controls and internal controls common to the components, and in testing the operational effectiveness of these controls.
- (c) Whether the group auditor, or other auditor, is required to issue a separate audit opinion on a component's financial statements.

Paragraph 44 provides guidance on the range of options available to the group auditor to obtain sufficient appropriate audit evidence in relation to the component's financial information.

Paragraphs 45 to 50 provide guidance on the practical application of the guidance in paragraphs 40, 43 and 44.

Some Task Force members were concerned that the guidance referred to above may be too prescriptive, while others were of the opinion that a need for this level of guidance exists.

IAASB Review of Proposed IAPS

The Task Force acknowledges that the wording and structure of the proposed IAPS requires further consideration by the Task Force. As a result, IAASB members are requested to focus their comments on the approach taken by the Task Force (i.e. with reference to the framework) and the appropriateness and completeness of the guidance provided.

Consideration should also be given as to whether or not inclusion of the framework as an appendix to the proposed IAPS may be helpful.

Timetable for Completion and Proposed Exposure of Pronouncements

The proposed revised ISA is submitted for final approval as an exposure draft at this meeting of the IAASB.

The Task Force intends to submit the proposed IAPS for approval as an exposure draft at the July 2003 IAASB meeting.

As the two documents are closely related, it is proposed that they are exposed at the same time, i.e. after the approval of the proposed IAPS in July 2003.

Material Presented

Agenda Paper 7-A (Pages 623 – 632)	Proposed Revised ISA 600 Considering the Work of Other Auditors (for approval as exposure draft)
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Agenda Paper 7-B (Pages 633 – 652)	Proposed IAPS on The Audit of Group Financial Statements (first read)
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Action Requested

1. The IAASB is asked to review and approve the proposed revised ISA 600 to be issued as an exposure draft.
2. IAASB is asked to review the proposed IAPS on The Audit of Group Financial Statements. Editorial comments should be forwarded to IAASB staff.

Attachment – Framework for the Development of the Proposed IAPS

[Distributed as separate PowerPoint file]

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