

**PROPOSED INTERNATIONAL AUDITING PRACTICE STATEMENT  
THE AUDIT OF GROUP FINANCIAL STATEMENTS  
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International Auditing Practice Statements (IAPS) XXXX, “The Audit of Group Financial Statements” should be read in the context of the “Preface to the International Standards on Quality Control, Auditing, Assurance and Related Services,” which sets out the application and authority of IAPSS.

## Introduction

### PURPOSE OF IAPS

1. This International Auditing Practice Statement (IAPS) provides practical assistance to auditors in applying International Standards on Auditing (ISAs) to the audit of group financial statements.
2. This IAPS is to be read in conjunction with proposed ISA 600 (Revised), “The Work of Other Auditors in the Audit of Group Financial Statements.”

### DEFINITIONS

3. The following terms have the meanings attributed below:
  - (a) “Applicable financial reporting framework” means the financial reporting framework applicable to the group financial statements.
  - (b) “Audit methodology” means the policies and procedures adopted by a firm and applied by the engagement team to perform audits of financial statements that are of a consistent quality.
  - (c) “Component” means a head office, parent, division, branch, subsidiary, joint venture, associated company or other entity whose financial information is or should be included in the group financial statements.
  - (d) “Component management” means management responsible for the preparation of the financial information of a component.
  - (e) “Group auditor” means the auditor<sup>1</sup> who signs the auditor’s report on the group financial statements.
  - (f) “Group financial statements” means financial statements that include or should include financial information of more than one component. The term “group financial statements” also refers to combined financial information aggregating the financial information of components in circumstances where there is no parent.
  - (g) “Group management” means management responsible for the preparation of the group financial statements.
  - (h) “Group-wide controls” means internal controls established by group management over group financial reporting.

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<sup>1</sup> The proposed revised “Glossary of Terms” (October 2004) defines auditor as follows: “The engagement partner. The term “auditor” is used to describe either the engagement partner or the audit firm. Where it applies to the engagement partner, it describes the obligations or responsibilities of the engagement partner. Such obligations or responsibilities may be fulfilled by either the engagement partner or a member of the audit team. Where it is expressly intended that the obligation or responsibility be fulfilled by the engagement partner, the term “engagement partner” rather than “auditor” is used. (The term “auditor” may be used when describing related services and assurance engagements other than audits. Such reference is not intended to imply that a person performing a related service or assurance engagement other than an audit need necessarily be the auditor of the entity’s financial statements.)”

- (i) “Other auditor” or “another auditor” means a related auditor or an unrelated auditor.
  - (j) “Parent” means the entity whose management prepares or should prepare group financial statements.
  - (k) “Related auditor” means an auditor from the group auditor’s firm or from a network firm that operates under common monitoring policies and procedures as contemplated in paragraph 87 of International Standard on Quality Control (ISQC) 1, “Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements.”<sup>2</sup>
  - (l) “Reporting package” ordinarily comprises standard formats to provide financial information for incorporation in the group financial statements. Reporting packages generally are not intended to be complete financial statements that provide a true and fair view of (or present fairly, in all material respects) the financial position and performance of the component in conformity with the applicable financial reporting framework.
  - (m) “Significant component” means a component that is of individual financial significance to the group or a component that has been identified at group level as likely to include significant risks of material misstatement of the group financial statements. (See proposed ISA 600 (Revised), paragraphs 8-10.)
  - (n) “Uniform accounting policies” means the specific principles, bases, conventions, rules and practices adopted by the group, based on the applicable financial reporting framework, and used by the components to report like transactions consistently.
  - (o) “Unrelated auditor” means an auditor other than the group auditor or a related auditor.
4. For purposes of this IAPS, reference to “consolidation” also includes the application of the equity method of accounting and the aggregation of the financial information of components in circumstances where there is no parent.

### Terms of Engagement

5. ISA 210, “Terms of Audit Engagements” contains standards and guidance on agreeing the terms of engagement with a client. In the case of an audit of group financial statements, the terms of engagement ordinarily:
- (a) Identifies the financial reporting framework applicable to the group financial statements;

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<sup>2</sup> ISQC 1, paragraph 87 reads as follows:

“Some firms operate as part of a network and, for consistency, may implement some or all of their monitoring procedures on a network basis. Where firms within a network operate under common monitoring policies and procedures designed to comply with this ISQC, and these firms place reliance on such a monitoring system:

- (a) At least annually, the network communicates the overall scope, extent and results of the monitoring process to appropriate individuals within the network firms;
- (b) The network communicates promptly any identified deficiencies in the quality control system to appropriate individuals within the relevant network firm or firms so that the necessary action can be taken; and
- (c) Engagement partners in the network firms are entitled to rely on the results of the monitoring process implemented within the network, unless the firms or the network advises otherwise.”

- (b) Specifies that the communication between the group auditor and other auditors will be unrestricted;
  - (c) Specifies that important communications between other auditors and component management, including communications on material weaknesses in internal control, will be made available to the group auditor;
  - (d) Specifies that important communications between regulatory authorities and components related to financial reporting matters will be made available to the group auditor; and
  - (e) Specifies that, to the extent that the group auditor considers it necessary, the group auditor will be permitted to have access to component information, component management and the other auditors, including their audit documentation, and to perform work on the financial information of the components.
6. The group auditor includes in the terms of engagement the fact that restrictions on the group auditor's access to component information, component management or the other auditors, or on the work to be performed on the financial information of a component, imposed after the group auditor's acceptance of the engagement to audit the group financial statements, will constitute a scope limitation that may affect the group auditor's report on the group financial statements or the group auditor's appointment. (See proposed ISA 600 (Revised), paragraphs 22-23.)

**Obtaining an Understanding of the Group, Its Components, and Their Environments, and of the Consolidation Process**

7. Proposed ISA 600 (Revised), paragraph 39, requires the group auditor to obtain an understanding of the group, its components, and their environments, and of the consolidation process, and to assess the risks of material misstatement of the group financial statements at group level. ISA 315, "Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement" contains standards and guidance on the understanding to be obtained of an entity and its environment and the assessment of risks of material misstatement. The application of ISA 315 in an audit of group financial statements is affected by the fact that the group auditor's understanding and risk assessment includes a number of components, and that other auditors may perform the work on the financial information of some of these components.
8. The nature, timing and extent of the risk assessment procedures to obtain an understanding of the group, its components, and their environments, and of the consolidation process depend on the group auditor's preliminary understanding of the group, its components, and their environments (see proposed ISA 600 (Revised), paragraphs 5-10) and the group auditor's experience with the group. The group auditor performs the following risk assessment procedures:
- (a) Inquiries of group management, internal audit, and those responsible for the consolidation and preparation of the group financial statements.
  - (b) Application of analytical procedures to financial information prepared at the group level and at the component level.

- (c) Observation and inspection of group-wide controls (see paragraph 10) and controls relevant to the consolidation.

#### MATTERS ABOUT WHICH THE GROUP AUDITOR OBTAINS AN UNDERSTANDING

##### *Group Control Environment*

9. The group auditor obtains an understanding of the group control environment. The group control environment includes the attitude, awareness and actions of those charged with governance and management concerning the group-wide controls and their importance in the group.
10. The group auditor obtains an understanding of group-wide controls in order to perform the risk assessment at group level (see paragraph 7), and to determine the audit procedures to be performed on the consolidation and the scope of work to be performed by the group auditor or other auditors on the financial information of the components. Group-wide controls may include a combination of the following:
- Regular meetings between group management and component management to discuss business developments and to review performance.
  - Monitoring components' operations and the results thereof, including regular reporting routines, enabling group management to monitor components' performance against budgets, and to take appropriate action.
  - Group management's risk assessment process, i.e., the process for identifying, analyzing and managing business risks, including the risk of fraud, that may result in material misstatement of the group financial statements.
  - Monitoring, controlling, reconciling and eliminating intra-group transactions and unrealized profits and intra-group account balances at group level.
  - A process for monitoring the timeliness and assessing the accuracy and completeness of financial information received from components.
  - A central IT system controlled by the same general IT controls for all or part of the group.
  - Control activities within an IT system that is common for all or some components.
  - Monitoring of controls, including activities of internal audit and self-assessment programs.
  - Consistent policies and procedures, including a group financial reporting procedures manual.
  - Group-wide programs, such as codes of conduct and fraud prevention programs.
  - Arrangements for the assignment of authority and responsibility to component management.
11. Where internal audit is regarded as part of group-wide controls, for example a centralized internal audit function as opposed to a decentralized internal audit function, and the group auditor plans to use the work of internal audit, the group auditor evaluates the competence and objectivity of the internal auditors.

12. Obtaining an understanding of group-wide controls involves evaluating their design and determining whether they have been implemented. When the group auditor intends to use information about group-wide controls obtained in prior periods, the group auditor makes inquiries of group management and performs other audit procedures, such as walk-through tests, to determine whether changes have occurred that may affect the relevance of such information in the current audit of the group financial statements.

#### *Components and Their Environments*

13. The group auditor determines the extent of the understanding required of the components and their environments. The group auditor's primary consideration is whether the group auditor's own understanding is sufficient to confirm the group auditor's initial identification of significant components (see proposed ISA 600 (Revised), paragraph 7(a)).

#### *Consolidation Process*

14. The group auditor obtains an understanding of the consolidation process, including controls relevant to the consolidation. The group auditor's understanding includes the following:

Matters relating to the applicable financial reporting framework, including the following:

- The extent to which component management has an understanding of the applicable financial reporting framework.
- The process for identifying and accounting for components in accordance with the applicable financial reporting framework.
- The process for identifying reportable segments for segment reporting in accordance with the applicable financial reporting framework.
- The process for identifying related party relationships and related party transactions for reporting in accordance with the applicable financial reporting framework.
- The accounting policies applied in the group financial statements, changes from those of the previous financial year, and changes as a result of new or revised standards under the applicable financial reporting framework.
- The procedures for dealing with components that have financial year-ends different from that of the group.

Matters relating to the consolidation process, including the following:

- Group management's process for obtaining an understanding of the accounting policies used by components, and for ensuring that uniform accounting policies are used to prepare the financial information of the components for purposes of the group financial statements and differences in accounting policies are identified and, where required in terms of the applicable financial reporting framework, adjusted.
- Group management's process for ensuring complete, accurate and timely financial reporting by the components for purposes of the consolidation
- The process for translating the financial information of foreign components into the currency of the group financial statements.

- The organization of IT for purposes of the consolidation, including the manual and automated stages of the process and the manual and programmed controls in place at the various stages of the consolidation process.
- Group management's process for obtaining information on subsequent events.

Matters relating to consolidation adjustments, including the following:

- The process for recording consolidation adjustments, including the preparation, authorization and processing of related journal entries, and the experience of personnel responsible for the consolidation.
  - The consolidation adjustments required in terms of the applicable financial reporting framework.
  - Business rationale for the events and transactions that gave rise to the consolidation adjustments.
  - Frequency, nature and size of transactions between components.
  - Procedures for monitoring, controlling, reconciling and eliminating intra-group transactions and unrealized profits and intra-group account balances.
  - Steps taken to arrive at the fair value of acquired assets and liabilities, procedures for amortizing goodwill (where applicable) and impairment testing of goodwill in accordance with the applicable financial reporting framework.
  - Arrangements with a majority owner or minority interests regarding losses incurred by a component (for example, an obligation of the minority interest to make good such losses).
15. In order to achieve uniformity and comparability of financial information, group management may issue financial reporting procedures manuals, reporting packages and related instructions to components, specifying the requirements relating to the financial information of the components to be included in the group financial statements. The instructions ordinarily cover the accounting policies to be applied, statutory and other disclosure requirements applicable to the group financial statements, including the identification and reporting of segments, related party relationships and transactions, intra-group transactions and unrealized profits and intra-group account balances, and a reporting timetable.
16. The group auditor ordinarily considers the proposed reporting package at an early stage of the audit of the group financial statements to determine whether it will provide sufficient appropriate information to prepare and present the group financial statements. The group auditor's consideration may include the following:
- The clarity and practicality of the instructions for completion of the reporting package.
  - The likelihood of component management having an understanding of the applicable financial reporting framework.
  - Whether the reporting package provides for:



- Disclosures sufficient to comply with the requirements of the applicable financial reporting framework, for example disclosure of related party relationships and transactions, and segment information;
- The identification of consolidation adjustments, for example intra-group transactions and unrealized profits and intra-group account balances; and
- Approval of the completed package by component management.

### *Fraud*

17. ISA 240 (Revised), “The Auditor’s Responsibility to Consider Fraud in the Audit of Financial Statements” contains standards and guidance on the auditor’s responsibility with regard to fraud. In the case of an audit of group financial statements, the group auditor obtains an understanding of the following:
- (a) Group management’s assessment of the risks that the group financial statements may be materially misstated as a result of fraud.
  - (b) Group management’s process for identifying and responding to the risks of fraud in the group, including any specific fraud risks that group management has identified or account balances, classes of transactions or disclosures for which a risk of fraud may be likely to exist.
  - (c) Whether there are particular components for which a risk of fraud may be likely to exist.
  - (d) How those charged with governance of the group exercise oversight of group management’s processes for identifying and responding to the risks of fraud in the group, and of the controls that group management has established to mitigate these risks.
18. The group auditor inquires of those charged with governance of the group, group management, internal audit and, if considered appropriate, component management, other auditors and others whether they have knowledge of any actual, suspected or alleged fraud affecting a component or the group.

### *Laws and Regulations*

19. ISA 250, “Consideration of Laws and Regulations in an Audit of Financial Statements” contains standards and guidance on the auditor’s responsibility to consider laws and regulations in an audit of financial statements. In the case of an audit of group financial statements, the group auditor obtains a general understanding of the laws and regulations applicable to the parent that may affect the group financial statements. Where another auditor will perform the work on the financial information of a component, the group auditor communicates laws and regulations applicable to the parent, and relevant to the work to be performed by the other auditor, to the other auditor. The group auditor also requests the other auditor to communicate to the group auditor instances of non-compliance with laws and regulations applicable to the component that could have a material effect on the group financial statements.

**Discussion Among Engagement Team Members Regarding the Risks of Material Misstatement of the Group Financial Statements, Including Risks of Fraud**

20. ISA 315 and ISA 240 (Revised) require the members of the engagement team to discuss the susceptibility of an entity to material misstatement of the financial statements due to fraud or error, with a specific emphasis on the risks of material misstatement due to fraud. The group auditor uses professional judgment, prior experience with the group and knowledge of current developments to determine who is included in the discussions, how and when they occur, and the extent of the discussions. In the case of an audit of group financial statements there may also be discussions that involve the group auditor and other auditors or key members of their teams.
21. The group auditor, or a related auditor on behalf of the group auditor, holds discussions with other auditors, or key members of their teams, who perform work on the financial information of significant components.
22. These discussions provide an opportunity to:
  - Share knowledge of the components and their environments, including group-wide controls.
  - Exchange information about the business risks to which the components or the group are subject.
  - Exchange ideas about how and where the group financial statements may be susceptible to material misstatement due to fraud or error, how group management and component management could perpetrate and conceal fraudulent financial reporting, and how assets of the components could be misappropriated.
  - Identify practices followed by group management or component management to manage earnings that could lead to fraudulent financial reporting, for example revenue recognition practices that are not in accordance with the applicable financial reporting framework.
  - Consider the known external and internal factors affecting the group that may create an incentive or pressure for group management, component management or others to commit fraud, provide the opportunity for fraud to be perpetrated, and indicate a culture or environment that enables group management, component management or others to rationalize committing fraud.
  - Consider the risk of group management or component management overriding controls.
  - Consider whether uniform accounting policies are used to prepare the financial information of the components for purposes of the group financial statements and whether differences in accounting policies are identified and, where required in terms of the applicable financial reporting framework, adjusted.
  - Discuss fraud that has been identified in components or information that has been obtained that indicates that a fraud may exist in a component.
  - Share information that may indicate non-compliance with national laws or regulations, for example payments of bribes and transfer pricing practices.

**Assessing the Risks of Material Misstatement of the Group Financial Statements**

23. The group auditor uses the information obtained from the understanding of the group, its components, and their environments, and of the consolidation process, including audit evidence obtained in evaluating the design and implementation of group-wide controls and controls relevant to the consolidation, and information obtained through discussions with other auditors (see paragraphs 20-22), to assess the risks of material misstatement of the group financial statements.
24. Examples of conditions or events that may indicate risks of material misstatement of the group financial statements, including risks of fraud, include the following:
- A complex group structure, especially where there are frequent acquisitions, disposals or reorganizations.
  - Poor corporate governance structures, including decision-making processes that are not transparent.
  - Non-existent or ineffective group-wide controls, including inadequate group management information to monitor components' operations and the results thereof.
  - Components operating in foreign jurisdictions that may be exposed to factors such as unusual government intervention in areas such as trade and fiscal policy, and restrictions on currency and dividend movements; and fluctuations in exchange rates.
  - Business activities of components that involve high risk, such as long-term contracts or trading in innovative or complex financial instruments.
  - Uncertainties regarding which components require incorporation in the group financial statements in accordance with the applicable financial reporting framework, for example, the existence of special purpose entities or non-trading entities.
  - Related party relationships and transactions (see paragraph 25).
  - Prior occurrences of intra-group account balances that did not balance or reconcile on consolidation.
  - Components' application of accounting policies that are not uniform with those applied in the group financial statements.
  - Components with different financial year-ends, which may be utilized to manipulate the timing of transactions.
  - Prior occurrences of unauthorized or incomplete consolidation adjustments.
  - Aggressive tax planning within the group or large cash transactions with entities in tax havens.
  - Multiple other auditors engaged to audit the financial information of the components and frequent changes of these auditors within the group.
25. ISA 550, "Related Parties" contains standards and guidance on the auditor's responsibilities regarding related parties and transactions with such parties. In the case of a complex group structure, there is a risk that related parties and related party transactions may not be identified. Consequently, it is important that, in assessing the risks of material

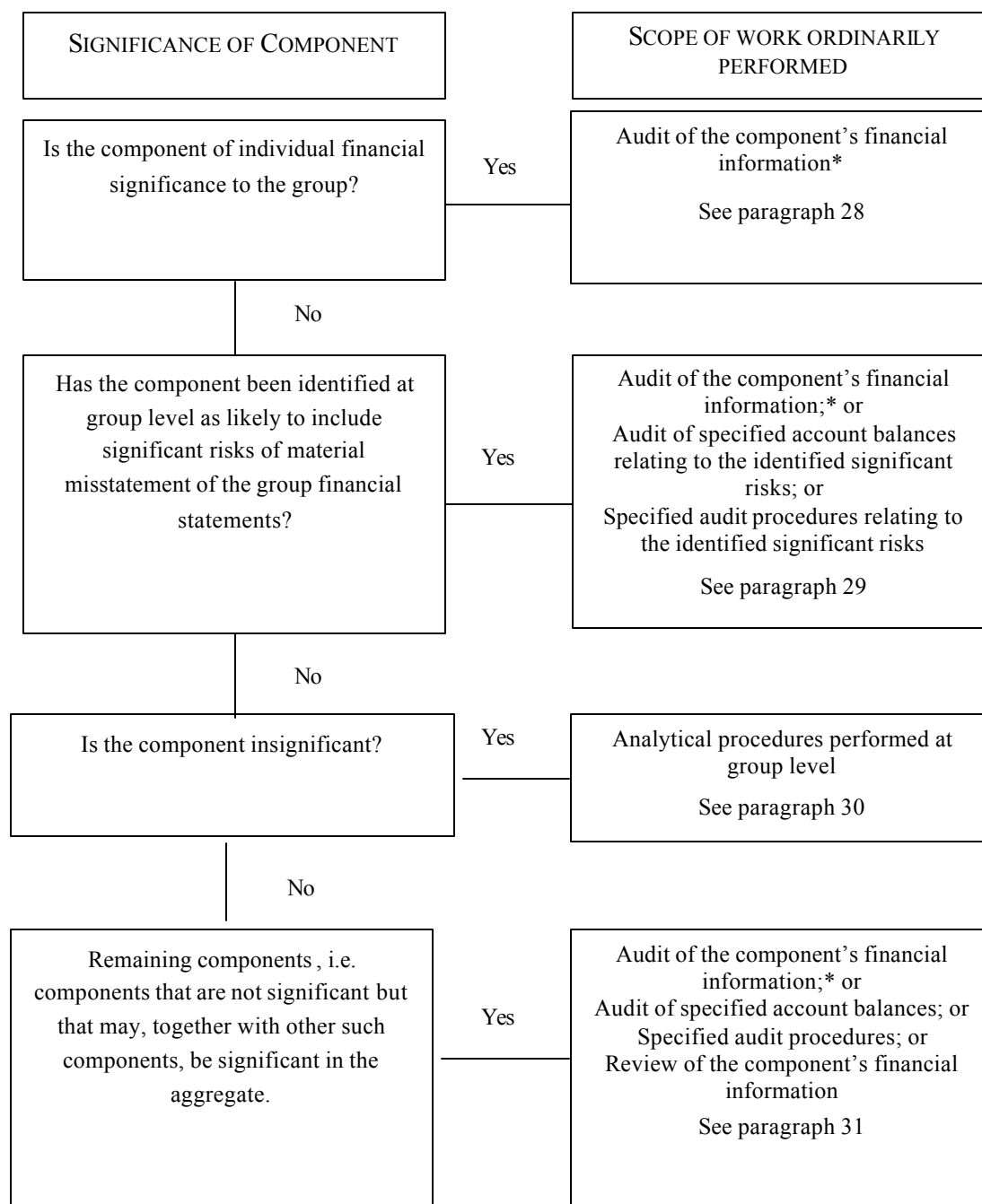
misstatement of the group financial statements, the group auditor is alert for transactions that appear unusual in the circumstances and may indicate the existence of previously unidentified related parties.

### **Responding to Assessed Risks**

26. Proposed ISA 600 (Revised), paragraph 41, requires the group auditor to determine the audit procedures to be performed on the consolidation and the scope of work to be performed by the group auditor or other auditors on the financial information of the components to respond to the assessed risks of material misstatement of the group financial statements. ISA 330, “The Auditor’s Procedures in Response to Assessed Risks” contains standards and guidance on determining overall responses and designing and performing further audit procedures to respond to the assessed risks of material misstatement.

### **DETERMINING THE SCOPE OF WORK TO BE PERFORMED ON THE FINANCIAL INFORMATION OF COMPONENTS**

27. The scope of work to be performed on the financial information of a component will be affected by matters such as the significance of the component, and the group auditor’s evaluation of the design and implementation of group-wide controls (see paragraph 10). The diagram below illustrates how the group auditor may decide on the scope of work to be performed on the financial information of the components.



Before finalizing the scope of work to be performed on components' financial information, the group auditor considers whether sufficient appropriate audit evidence will be obtained to enable the group auditor to express an audit opinion on the group financial statements (see paragraph 33)

\*Performed in accordance with ISAs using either a materiality level determined by the group auditor or a lower materiality level determined by the other auditor.

*Significant Components*

28. For a component that is of individual financial significance (see proposed ISA 600 (Revised), paragraph 9), the group auditor ordinarily performs or requests other auditors to perform an audit in accordance with ISAs using either a materiality level determined by the group auditor, or a lower materiality level determined by the other auditor.
29. For a component that has been identified at group level as likely to include significant risks of material misstatement of the group financial statements (see proposed ISA 600 (Revised), paragraph 10), the group auditor ordinarily performs or requests other auditors to perform one of the following:
  - An audit in accordance with ISAs using either a materiality level determined by the group auditor, or a lower materiality level determined by the other auditor.
  - An audit of specified account balances relating to the identified significant risks.
  - Specified audit procedures relating to the identified significant risks.

*Insignificant Components*

30. After determining the scope of work to be performed on the financial information of components that are of individual financial significance (see paragraph 28) and components identified at group level as likely to include significant risks of material misstatement of the group financial statements (see paragraph 29), the group auditor identifies components that are insignificant, even when aggregated with other such insignificant components. As discussed in proposed ISA 600 (Revised), paragraph 9, the group auditor may apply a percentage to a chosen benchmark as a step in identifying the individual financial significance of components. While in practice there are ranges of possible percentages, a component representing less than 2% of group assets, liabilities, cash flows, profit or turnover will ordinarily be regarded insignificant. The group auditor may consider it appropriate not to perform audit or review procedures at insignificant components. For these components, the group auditor ordinarily performs analytical procedures at group level.

*Components That may be Significant in the Aggregate*

31. The remaining components, although not significant due to their size or risk, may, together with other such components, be significant in the aggregate. The scope of work to be performed on the financial information of such components could include one of the following:
  - An audit performed in accordance with ISAs using either a materiality level determined by the group auditor, or a lower materiality level determined by the other auditor.
  - An audit of specified account balances.
  - Specified audit procedures.
  - A review of the financial information of the component.

The scope of work to be performed on the financial information of these components is affected by matters such as the following:

- Whether it is a newly formed or acquired component.
  - Whether significant changes have taken place in the component.
  - Whether internal audit has performed work at the component.
  - The effectiveness of group-wide controls.
  - The individual financial significance of and risks posed by the component in comparison with other components within this category.
32. For example, analytical procedures performed at group level might have indicated a significant increase in sales and accounts receivables. Discussions with group management revealed that the increase is due to the establishment of a new market for one of the group's products. The new market was established in a country with severe economic problems, which might affect the collection of the accounts receivables. The group auditor determined that the product is manufactured and sold by three of the group subsidiaries. Although these subsidiaries are not significant by themselves, they might be in the aggregate. Based on the group auditor's risk assessment performed at group level (see paragraph 7), the group auditor performs, or requests the other auditors to perform, an audit of the accounts receivables at these three components.

*Sufficient Appropriate Audit Evidence*

33. Before finalizing the scope of work to be performed on the financial information of the components, the group auditor considers whether sufficient appropriate audit evidence will be obtained to enable the group auditor to express an audit opinion on the group financial statements. Accordingly, the scope of work to be performed on the financial information of the components includes audits performed in accordance with ISAs using either a materiality level determined by the group auditor, or a lower materiality level determined by the other auditor; audits of specified account balances; and specified audit procedures. For example, if none of the components are significant (as described in paragraphs 30-31), the group auditor cannot limit the scope of work to be performed on the financial information of the components to reviews, or analytical procedures performed at group level.

*Components Subject to Audit by Statute, Regulation or for Another Reason*

34. The financial statements of a component may be subject to an audit because of statute, regulation or other reason. This may affect the group auditor's decision on the work to be performed on the financial information of the component for the purposes of the audit of the group financial statements. The group auditor may decide to use this audit to provide audit evidence for the purposes of the audit of the group financial statements. In such circumstances, the group auditor evaluates the effect of the financial reporting framework applied in the preparation of the financial statements of the component and the auditing standards applied by the other auditors. The auditor also considers whether the audit of the financial statements of the component will be performed in time for the other auditor's report or memorandum to be communicated to the group auditor (see proposed ISA 600 (Revised), paragraph 65).
35. When the group auditor decides to use the audit of the financial statements of a component performed by another auditor to provide audit evidence for purposes of the audit of the

group financial statements, and the risk assessment procedures and further audit procedures have already been performed by the other auditor at the component (for example in the case of a component acquired close to the group reporting date), the group auditor, in order to meet the requirements described in proposed ISA 600 (Revised) paragraphs 51-58, reviews the risk assessment procedures and further audit procedures already performed, and determines the additional audit procedures to be performed.

## **Performing Further Audit Procedures**

### **TESTING INTERNAL CONTROLS**

36. The group auditor's risk assessment at group level (see paragraph 7) and the group auditor's determination of the scope of work to be performed on the financial information of the components (see paragraphs 27-35) may be based on an expectation that group-wide controls are operating effectively. Where there is such an expectation, the group auditor performs, or requests another auditor to perform, tests of the operating effectiveness of the controls. When the group-wide controls include a central IT system that is controlled by the same general IT controls, for example at a shared service center, the group auditor tests the operating effectiveness of those controls centrally. When the control activities of an IT system are common for all or some components, the group auditor may obtain audit evidence relevant to those components from testing, or requiring another auditor to test, the control activities for one or more components.

### **CONSOLIDATION**

37. The consolidation process may require adjustments to amounts reported in the group financial statements that do not pass through the usual transaction processing systems and that may not be subject to the same internal controls that other financial information is subject to. These adjustments typically comprise consolidation adjustments and reclassifications. The group auditor assesses the risks of material misstatement of the group financial statements arising from the consolidation and determines the work to be performed on the consolidation accordingly. The group auditor:
- (a) Considers the appropriateness and completeness of the consolidation adjustments, as well as the arithmetical accuracy of calculations;
  - (b) Considers whether the consolidation adjustments appropriately reflects the events and transactions underlying the adjustments;
  - (c) Determines whether significant adjustments have been correctly processed, have been authorized by group management and, where applicable, by component management and are supported by sufficient appropriate documentation; and
  - (d) Checks the reconciliation and elimination of intra-group transactions and unrealized profits and intra-group account balances.
38. Inconsistent accounting policies may exist where components operate in diverse industry segments or are located in jurisdictions that require different financial reporting frameworks. If required in terms of the applicable financial reporting framework, such inconsistencies ordinarily will be eliminated either by group management requiring components to prepare financial information consistent with the accounting policies



applied in the group financial statements, or by group management requiring component management to disclose the differences between the accounting policies applied in the financial information of the component and those applied in the group financial statements.

39. Where uniform accounting policies are required in terms of the applicable financial reporting framework and they have not been adopted by a component, the group auditor considers whether group management or component management has made appropriate adjustments to the financial information of the component for purposes of preparing and presenting the group financial statements. Where another auditor performs the work on the financial information of a component, the group auditor requests the other auditor to confirm to the group auditor that such adjustments have been made.
40. If the group financial statements include the financial statements of components with year-ends that differ from that of the group, the group auditor determines whether this is acceptable under the applicable financial reporting framework. The group auditor also considers the component's results between its financial year-end and the date of the group financial statements, and identifies significant transactions, including intra-group transactions and unrealized profits, or other events and disclosures that need to be reflected in or eliminated from the group financial statements. Where another auditor performs the work on the financial information of a component, the group auditor requests the other auditor to perform the procedures considered necessary by the group auditor under the circumstances.
41. Sometimes adjustments processed on consolidation relate to misstatements. Where such adjustments have not been processed in the relevant components' accounting records, the group auditor requests group management to have them processed appropriately.

#### MANAGEMENT REPRESENTATIONS

42. ISA 580, "Management Representations" and other ISAs, for example ISA 240 (Revised), contain standards and guidance on management representations. In the case of an audit of group financial statements, the group auditor also obtains written representations from group management, acknowledging its responsibility for:
  - The establishment and maintenance of internal controls, including controls over the preparation and presentation of the group financial statements;
  - The fair presentation of the group financial statements in accordance with the applicable financial reporting framework;
  - That all components have been included in the group financial statements in accordance with the applicable financial reporting framework;
  - That disclosures in the group financial statements are appropriate and complete, including that the disclosures of related party relationships and transactions and reportable segments are in accordance with the applicable financial reporting framework;
  - That accurate and complete financial information has been obtained from components; and

- That consolidation adjustments are appropriate and complete, including the elimination of intra-group transactions and unrealized profits and intra-group account balances, and, where required in terms of the applicable financial reporting framework, adjustments for inconsistent accounting policies.

### **Evaluating the Sufficiency and Appropriateness of Audit Evidence Obtained**

43. The group auditor evaluates whether sufficient appropriate audit evidence has been obtained from the audit procedures performed on the consolidation and the work performed on the financial information of the components on which to base the audit opinion on the group financial statements. This evaluation includes the work performed by other auditors.
44. If the group auditor concludes that sufficient appropriate audit evidence has not been obtained, the group auditor obtains further audit evidence, if possible. In the case of components on which other auditors performed the work, the group auditor may request the other auditors to perform additional procedures or, if this is not feasible, perform the group auditor's own procedures on the financial information of the components. When the group auditor has not been able to perform sufficient additional audit procedures, the group auditor considers the effect of this scope limitation on the auditor's report on the group financial statements.

### **Communication With Group Management and Those Charged With Governance**

#### **COMMUNICATION WITH GROUP MANAGEMENT**

45. The group auditor makes group management aware, as soon as practical and at an appropriate level of responsibility, of material weaknesses in the design or operation of group-wide controls and in controls over the preparation and presentation of the group financial statements. The group auditor also makes group management aware of material weaknesses in internal controls at components that have been identified by the group auditor, or that have been brought to the attention of the group auditor by other auditors, and that the group auditor judges are of significance in the context of the group.
46. If fraud has been identified in components or information has been obtained that indicates that a fraud may exist in a component, the group auditor communicates these matters as soon as practicable to group management. If the group auditor believes or suspects that group management may be involved in the fraud, the group auditor communicates the matters to those charged with governance.

#### **COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE**

47. ISA 260, "Communication With Those Charged With Governance" and other ISAs, for example ISA 240 (Revised), contain standards and guidance on communication with those charged with governance. Communication with those charged with governance of the group takes place at various times during the audit of the group financial statements. The matters that the group auditor communicates to those charged with governance of the group include those matters brought to the attention of the group auditor by other auditors that the group auditor judges to be of governance significance in the context of the group.

### **Communication With Another Auditor Who is Required to Audit the Financial Statements of a Component**

48. Where another auditor is required by statute, regulation or for another reason to express an audit opinion on the financial statements of a component and the group auditor becomes aware of matters that may be significant to the financial statements of the component that component management may be unaware of, the group auditor considers requesting group management to inform component management of such matters. Examples of such matters include the following:
- Potential litigation.
  - Plans for abandonment of material operating assets.
  - Subsequent events.
  - Significant legal agreements.
49. There may be occasions when group management may need to keep confidential certain material sensitive information. In these circumstances the group auditor ordinarily discusses with group management the risk of component management issuing misleading financial statements, and requests group management to communicate to component management that they should not issue the financial statements of the components. In addition, the group auditor may consider it necessary to communicate to the other auditor that they should not issue the auditor's report on the financial statements of the component until such time as group management has resolved the outstanding matter. When group management remains of the opinion that the matter should not be communicated to component management, the group auditor considers resigning from the engagement.

**Effective Date**

50. This IAPS is effective on first application of proposed ISA 600 (Revised).

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