

Group Audits – Summary of Significant Comments and Task Force’s Recommended Dispositions**Introduction**

1. On May 17 a total of 40 comment letters have been received on the exposure draft of the proposed revised ISA 600, “The Work of Related Auditors and Other Auditors in the Audit of Group Financial Statements” and the proposed IAPS, “The Audit of Group Financial Statements.” (A list of respondents is included in Appendix 1.)
2. This paper summarizes significant comments received until May 17 for consideration by the IAASB during its June 2004 meeting. (Although the task force had the opportunity to consider a draft comment letter from the European Commission, it is still awaiting the final letter and, as a result, the Commission’s comments are not reflected in this summary.) The IAASB’s input at this stage is important to provide the task force with the direction necessary to appropriately dispose of the comments received, and to commence the revision of the proposed ISA and IAPS for consideration at the December 2004 IAASB meeting (see proposed timetable below).

Overall Support

3. Respondents were very supportive of the project to develop standards and guidance for the audit of group financial statements and acknowledged that they fill an important gap in the existing ISAs. Although some respondents were of the view that the proposed standards and guidance will assist auditors in performing quality audits of group financial statements (while others indicated that it confirmed current best practice), many respondents asked that the group auditor’s responsibilities are further clarified and strengthened. The calls for more rigor were based on recent corporate scandals.

Significant Comments

4. Significant comments on the following subject matters are summarized below. Each subject matter is followed by the task force’s recommended disposition.
 - (a) Sole vs. divided responsibility (paragraphs 5 – 20 and Appendix 2)
 - (b) Related auditor vs. other auditor (paragraphs 21 – 24)
 - (c) Acceptance and continuance as group auditor (paragraphs 25 – 29)
 - (d) ISA vs. IAPS (paragraphs 30 – 35)

SOLE VS. DIVIDED RESPONSIBILITY

5. The table below provides an overview of the comments received on the approach followed in the ISA with regard to sole responsibility and divided responsibility.

Retain provisions for sole responsibility and divided responsibility, i.e. “as is”	3
Countries that do not permit divided responsibility should be able to make the necessary adjustment to the ISA to eliminate it in their national standard	2
Retain provisions for sole responsibility and divided responsibility, but strengthen requirements for /	2

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provide more guidance on sole responsibility / divided responsibility	
Provide for sole responsibility as preferred method and divided responsibility as allowed alternative	1
Provide for sole responsibility as preferred method and divided responsibility as allowed alternative, but work towards elimination of allowed alternatives	2
Provide for sole responsibility as preferred method and divided responsibility as allowed alternative in ISA, and provide additional guidance on divided responsibility in a separate IAPS	1
Permit divided responsibility only when <i>required</i> by national law	2
Permit divided responsibility only when sole responsibility is not permitted	1
Permit divided responsibility only in very limited circumstances	3
Retain provisions for sole responsibility and divided responsibility, but the performance requirements for the group auditor should be same under both approaches	3
Provide for sole responsibility only	16
No specific mention of matter	4
TOTAL	40

6. Although the European Commission has not yet submitted a final comment letter, it is clear from the proposed 8th Directive that it favors sole responsibility.
7. Respondents opposing divided responsibility strongly encouraged the IAASB to revisit the proposed position regarding divided responsibility. They did not believe that giving equal recognition to both sole and divided responsibility shows the leadership that a global standard setter should be taking on this issue, and was concerned that this may affect the recognition of the IAASB as a credible and recognized international standard setter. Furthermore, they believed that sole responsibility was in the best interest of promoting high quality audits, and that pressure on national standards and regulations could help to reach the main intention of the IAASB, i.e. to promote consistent practices by auditors worldwide. They were of the opinion that the facilitation of convergence of national standards with international standards should not be at the expense of making compromises that fundamentally weaken ISAs.
8. Many arguments against and supporting divided responsibility were given. These are summarized in Appendix 2.
9. Two respondents were of the view that the procedures to be performed by the group auditor are not sufficient to take sole responsibility for the audit of the group financial statements, and that the standards and guidance in the ISA could be strengthened mostly by moving guidance from the IAPS to ISA, and by developing additional requirements for the group auditor.
10. Three respondents were of the view that the procedures to be performed by the group auditor should be the same, irrespective of sole or divided responsibility, and that the only difference between the two approaches should be the reference to the other auditor in the auditor's report. In addition, these respondents were of the view the procedures to be performed by the group auditor should be strengthened as discussed in paragraph 9 above.
11. Some respondents supporting divided responsibility were of the opinion that the related standards and guidance should be expanded. Recommendations included the following:

- Guidance should be provided as to when the IAASB believes divided responsibility is more appropriate than sole responsibility, and when sole responsibility is more appropriate than divided responsibility.
- The ISA should be redrafted in such a way that national standards determine whether and the extent to which it is possible to use divided responsibility, and that ISAs determine the work that the group auditor should do in the case of divided responsibility. This would allow for consistency in the application of ISAs to group audits.
- In order for an effective audit to be achieved under divided responsibility, the following standards and guidance should be included:
 - The group auditor should audit a significant portion of the group;
 - The group auditor should be satisfied as to the reputation, ethical characteristics and independence of the other auditor; and should obtain acknowledgements from the other auditor that the other auditor is independent and aware that the group auditor will refer to his audit of the component's financial information in the group auditor's report;
 - The group auditor should determine that the other auditor has the appropriate auditing and financial reporting skills and competence;
 - There should be interactive communications between the group auditor and the other auditor, including an exchange of knowledge of existing relationships (including the names of known related parties, and the extent of group and component management involvement in material transactions), and discussion of significant matters (including significant risks at the component) and of the other auditor's findings;
 - The group auditor should inquire of the other auditor with regards to uncorrected misstatements and material weaknesses in internal control and evaluate the effect of such matters on the group financial statements;
 - Each of the component audits being referred to should have been conducted at a level of materiality appropriate to the components and not at a level of materiality greater than the materiality of the group;
 - The group auditor should obtain a letter of representation from the other auditor as to whether his audit of the component revealed matters that, in his or her opinion, might have a material effect on the group financial statements and would require disclosure in the notes thereto; and
 - The group auditor should obtain an auditor's report issued in accordance with the ISAs from the other auditor.
- The division of responsibility should be made transparent to the users of the financial statements through the auditor's report. The ISA should include an example of an auditor's report that makes reference to the work of the other auditor. The group auditor's report should:
 - Disclose that the alternative method of divided responsibility has been chosen;

- Disclose the different components of the group financial statements, indicating those audited by the group auditor and those audited by other auditors, as well as the magnitude of the portion of the group financial statements of each such component; and
 - Identify the other auditors, unless this is clearly done in the group financial statements. (One respondent was of the view that, at a minimum, the names, places of operation and qualifications of the other auditors should be disclosed.)
- The standard should not give a choice over the basis for showing the magnitude of the portion of the group financial statements audited by other auditors – instead, all criteria listed should be disclosed.
12. Three respondents were of the view that there may be exceptional circumstances when it would be impracticable for the group auditor to accept sole responsibility for the work of another auditor. For example, this would not be possible in situations where an entity makes a major acquisition just before the entity's accounting year-end and, given time constraints for filing of the audited group financial statements, it is not possible for the group auditor to perform the procedures necessary to obtain sufficient appropriate audit evidence regarding the work performed by the incumbent component auditor. There may also be circumstances when the group auditor is not given access to a component or the component auditor's working papers.
13. In such circumstances, the group auditor is faced with a limitation in the scope of work necessary to accept sole responsibility and, as suggested in the ISA, needs to consider the impact of that limitation on the group auditor's opinion and report. The respondents noted that in some jurisdictions and circumstances, a scope limitation may not be a viable option and dividing responsibility in the auditor's report may be the only practical way of dealing with the limitation. To accommodate these practical limitations, it was recommended that guidance should be added to the section on reporting to allow the group auditor to refer to another auditor in the auditor's report in exceptional circumstances when it is impracticable or not possible for other reasons for the group auditor to accept sole responsibility for the work of another auditor.
14. One respondent was of the view that audits conducted under one quality control process and audit methodology best protect the public interest. By involving only one auditor (including related auditors) communications will be improved and better consistency of audit procedures achieved. Accordingly, the respondent believed that there usually should be only one auditor involved in an audit of group financial statements. Although the respondent did not believe that the auditing standards should mandate that one auditor perform the entire audit, the respondent believed that those charged with governance and auditors should critically evaluate the reasons for having multiple auditors and whether using multiple auditors is consistent with appropriate audit effectiveness. However, the respondent did recognize that there are legitimate circumstances in which the use of only one auditor is not feasible, for example in the case of an acquisition or joint venture. In these situations, it was believed that the group auditor must perform more stringent, additional procedures than those currently proposed in the ISA.
15. Respondents also recommended that the word "full" should be used in both the ISA and IAPS instead of "sole," as this term better articulates the concept that the group auditor is taking

responsibility for the work of others. The word “sole” can be defined as “having no sharer,” “being the only one,” “functioning independently and without assistance or interference,” all of which imply that other auditors were not involved at all, which is not the case in most circumstances when the group auditor takes “sole responsibility.”

Task Force Deliberations and Recommended Disposition

16. The task force reviewed the comments received on sole vs. divided responsibility. The task force recommends that:

- (a) The ISA should be revised not to distinguish between sole and divided responsibility.
- (b) The group auditor’s procedures should be the same whether he accepts sole or divided responsibility.
- (c) The group auditor’s procedures should be strengthened – mostly by moving guidance from the IAPS to the ISA, and by developing additional requirements for the group auditor. (See paragraph 35 below.) The IAPS should apply whether the group auditor accepts sole or divided responsibility.
- (d) The reporting section in the ISA should be redrafted to indicate that national law or standards may allow a group auditor to refer to another auditor in the auditor’s report on the group financial statements. However, such reference (1) should be in a separate emphasis of matter paragraph, and (2) does not affect the group auditor’s procedures (see (b) above). Should the group auditor be unable to obtain sufficient appropriate audit evidence in relation to a component, it will constitute a scope limitation and the group auditor will have to consider the effect of such scope limitation on the auditor’s report on the group financial statements. The group auditor will not be able to refer to the other auditor instead of qualifying his auditor’s report based on the scope limitation.

17. The task force is of the view that the recommended disposition is in line with the approach followed in developing the ISA and IAPS, i.e. that the group auditor is responsible for the audit of the group financial statements and, as a result, the decision of the scope of work to be performed and by whom such work should be performed. The task force also believes that it will enhance the group auditor’s consideration of the adequacy of the other auditors’ work, ensuring that the same audit quality and accountability are achieved in all circumstances.

18. The new audit risk model requires an auditor to obtain an understanding of the entity and its environment, perform a risk assessment, respond to the assessed risks, and obtain sufficient appropriate audit evidence to be able to express an opinion on the financial statements. Based on the recommended disposition, the proposed revised ISA and IAPS will continue to assist the group auditor in applying the new audit risk model to an audit of group financial statements. The ISA and IAPS will clarify that the group auditor’s obligation to obtain sufficient appropriate audit evidence to be able to express an opinion on the group financial statements is not affected by the fact that another auditor participates in the audit of the group financial statements, whether or not that auditor is referred to in the group auditor’s report.

19. The task force realizes that the recommended disposition may have the following potential implications:

- (a) Increase in audit fees (for both instances of sole responsibility and divided responsibility, as it is recommended that the group auditor's procedures under sole responsibility are strengthened too). However, a portion of the increase in audit fees may be a result of the implementation of the new audit risk model, as discussed in paragraph 17 above and the explanatory memorandum that accompanied the audit risk model exposure draft,
- (b) A move to appointing only one auditor for a majority of the components in a group and a resulting negative effect for small- and medium-sized practitioners (SMPs), and
- (c) An increase in qualified auditor's reports on group financial statements as a result of scope limitations, for example in the case of associated companies and joint ventures where the group auditor's access may be restricted. (It was noted that the Securities Exchange Commission in the US does not accept qualified auditor's reports.)

20. The task force is of the view that, should the IAASB accept the recommended disposition and agree on re-exposing the revised proposed ISA and IAPS, an explanatory memorandum should make readers aware of the potential implications of the revised proposed ISA and IAPS. To achieve this, it may be necessary for research to be conducted (before finalization of the exposure draft – see paragraph 36 below) to determine the potential increase in audit fees and scope limitations. It may also be necessary to consult directly with preparers, investors and SMPs. The Transnational Auditors Committee (TAC) and the Consultative Advisory Group (CAG) may be able to assist in this regard.

IAASB Action: Does the IAASB agree with the task force's recommended disposition and proposed way forward?

RELATED AUDITOR VS. OTHER AUDITOR

21. ISA 600.7(h) defines "related auditor" as "an independent auditor from the group auditor's office, other office of the group auditor's firm, a network firm or another firm operating under common quality control policies and procedures as described in International Standard on Quality Control (ISQC) 1, 'Quality Control for Audit, Assurance and Related Services Practices.'" 17 respondents commented on this definition. Significant comments, which recommended a "narrower" definition, included the following:

- An auditor from the group auditor's office should not be construed as a related auditor, as in these circumstances the group auditor acts as lead engagement partner over the auditor from the group auditor's office.
- The reference to "common quality control policies and procedures as described in ISQC 1" may imply that firms within the Forum of Firms are related auditors.
- Whilst many network firms operate under common quality control policies and procedures, there may be firms within a network that do not function as such due to legal or regulatory restrictions within the jurisdiction in which they operate.
- Based on the definition, two firms are "related" if they both comply with ISQC 1; however, they may have differing quality control policies and procedures. The definition should be

based on the fact that the quality control policies and procedures are the same, not that they comply with ISQC 1.

- The distinction between related auditors and other auditors, and the impact that it has on the group auditor's procedures in relation to their work, presume that the group auditor can rely on the quality control system of the related auditors' firm. This can only be done if the group auditor and related auditors share, at a minimum, common monitoring policies and procedures designed to help ensure that the related auditors' firms comply with ISQC 1.
- The term "related auditor" should be reserved for cases where that auditor is part of the same firm under common legal control and shares the same administrative and internal control policies and quality control system. The definition could possibly be extended to include a very closely affiliated firm that operates with a common set of operating control and quality control procedures and has agreements regarding cooperation and exchange of audit documentation and processes. Under these conditions a commonality of traits could exist to the extent that would be the case in a single firm. In any case, the definition should not include a firm that has only a marketing agreement or a referral agreement with the group auditor's firm. This point should hold even if another auditor has quality control policies and procedures that comply with ISQC 1.

22. Two respondents were of the view that requiring common quality control policies and procedures may be too restrictive, and that some flexibility should be allowed for situations where the group auditor is satisfied with the effectiveness of quality control policies and procedures that are not necessarily the same as the quality control policies and procedures of the group auditor. This would address situations where legal and regulatory requirements prevent common quality control policies and procedures. (The task force and IAASB have debated before whether the group auditor can determine the effectiveness of the quality control system of another auditor's firm, and agreed that it will be very difficult, if not impossible.)
23. Four respondents did not support the distinction in the ISA and IAPS between a related and other auditor, and the impact that the distinction has on the group auditor's procedures performed in relation to their work. One respondent was of the view that the distinction could be maintained, but that the group auditor and related auditors have to have common monitoring policies designed to ensure compliance with ISQC 1. Three respondents were of the view that the group auditor has to consider the professional qualifications, etc. (ISA 600.15) of related auditors and supervise their work. Another respondent was of the view that the group auditor should be required to determine whether another auditor in fact meets the definition of a related auditor before applying the distinction provided for in the ISA and IAPS.

Task Force Deliberations and Recommended Disposition

24. The task force reviewed the comments received on the definition of "related auditor" and the distinction between related auditors and other auditors. The task force recommends that:
- (a) "Related auditor" should be defined as "an independent auditor from the group auditor's firm or from a network firm that operates under common monitoring policies and procedures as described in paragraph 87 of ISQC 1." Paragraph 87 of ISQC 1 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) The ISA should clarify the fact that another auditor from a network firm, which does not operate under common monitoring policies and procedures as described in paragraph 87 of ISQC 1, is considered an “other auditor.”
- (c) To further support the distinction between related auditors and other auditors, and the fact that the group auditor’s procedures in relation to their work may differ, a new standard should be inserted in the ISA, requiring the group auditor to determine whether another auditor is in fact a related auditor. New guidance could deal with the link between the common monitoring policies and procedures (as described in paragraph 87 of ISQC 1) and the related auditor’s professional qualifications, etc. (ISA 600.16), as well as the matters referred to in ISA 600.18. The Professional Qualifications, Independence, Professional Competence, Resources and Quality Control Process ... section in the ISA, i.e. ISA 600.15-18, could then be limited to other auditors.
- (d) The guidance in the ISA should acknowledge that, in addition to common monitoring policies and procedures as described in paragraph 87 of ISQC 1, the group auditor and a related auditor may apply the same audit methodology. This may further affect the group auditor’s procedures in relation to the related auditor’s work, for example the group auditor may decide not to review the work of the related auditor. As a result, the ISA should explain the term “audit methodology” and clarify the group auditor’s procedures when (1) another auditor meets the definition of “related auditor,” (2) another auditor meets the definition of “related auditor” and applies the same audit methodology, and (3) when another auditor that is not a related auditor (i.e. other auditor) is to perform the work on a component’s financial information.

IAASB Action: Does the IAASB agree with the task force’s recommended disposition?

ACCEPTANCE AND CONTINUANCE AS GROUP AUDITOR

25. Respondents agreed that the group auditor should not accept or continue an engagement to report on the group financial statements if the group auditor and related auditors do not directly perform

a significant amount of the work on the group financial statements. Some were of the view that the standards and guidance on acceptance and continuance in the ISA should be strengthened by revising the related guidance in the IAPS and moving it to the ISA.

26. The majority of respondents that commented on the Acceptance and Continuance as Group Auditor sections of the ISA and IAPS opposed the “50% acceptance/retention proposal” (see IAPS.12). Most of them recommended deletion of the proposal.

Task Force Deliberations and Recommended Disposition

27. The task force reviewed the comments received on the Acceptance and Continuance as Group Auditor sections of the ISA and IAPS.

28. The task force agreed that ISA 600.8 is very wide and that IAPS.12 permits the auditor to accept an engagement where the group auditor and related auditors directly perform work on a small percentage of the group assets, liabilities, cash flows, profit or turnover, provided that the group auditor and related auditors are able to participate in the work of the other auditors. The majority of the task force members were also of the view that it was important to retain the “50% acceptance/retention proposal” in the guidance, as different firms may apply different benchmarks, which may have a negative effect on the quality of group audits. (One task force member did not support the retention of the proposal.)

29. The task force recommends that:

- (a) The guidance in IAPS.11-15 should be revised and combined with the standards and guidance in the ISA. Proposed wording for the revised standards and guidance to be included in the ISA is set out below. The task force acknowledges that it should give further consideration to the wording and that it may require amendment when read in the context of the other standards and guidance in the ISA. As a result, the IAASB is requested to consider the principles, rather than the exact wording.

1. **The group auditor should not accept an engagement to audit group financial statements unless the group auditor and related auditors directly perform work on a significant portion of the group assets, liabilities, cash flows, profit or turnover.**
2. In considering whether the group auditor and related auditors directly perform work on a significant portion, the group auditor takes account of the size (percentage) of the group assets, liabilities, cash flows, profit or turnover that the group auditor and related auditors directly perform work on, as well as the risks of material misstatement of the group financial statements. Other factors that may affect the group auditor’s decision as to whether to accept or continue an engagement to audit the group financial statements include the following:
 - The group structure and any changes since the previous audit, for example acquisitions, disposals or reorganizations.

- The components' business activities, including the regulatory, economic and political environments in which these activities take place and any changes since the previous audit.
 - Changes in group management or component management since the previous audit.
 - Whether the group auditor has experienced difficulties in the past with regard to the integrity and competence of group management or component management.
 - Risks of material misstatement, fraud risks and misstatements identified during the prior audits of the group financial statements.
 - Existence of group-wide controls and any changes since the previous audit.
 - The complexity of the group financial statements.
 - The professional qualifications, independence, professional competence and resources of the other auditors, and the quality control processes of the other auditors' firms.
 - Whether group management and component management will permit, or continue to permit, the group auditor to have unrestricted access to those charged with governance of the group, group management, component management, component information and the other auditor, including the other auditor's working papers, and to perform such additional work on the components' financial information as the group auditor may consider necessary.
3. A significant portion ordinarily is approximately, but rarely precisely, 50% of the group assets, liabilities, cash flows, profit or turnover, and may vary in different circumstances. It is important to understand the reasons why a group is choosing to engage multiple auditors, and the group auditor uses professional judgment in deciding whether to accept an engagement where the group auditor and related auditors will directly perform work on less than approximately 50%, or the percentage considered appropriate in the circumstances. The group auditor's decision will be affected by factors such as those listed in paragraph 2. Where the group auditor decides to accept an engagement where the group auditor and related auditors will directly perform work on less than approximately 50%, or the percentage considered appropriate in the circumstances, the group auditor attempts to increase the portion on which the group auditor and related auditors directly perform as soon as possible, or ordinarily does not continue the engagement in the following year. The group auditor and related auditors have to directly perform work on a significant portion of the group assets, liabilities, cash flows, profit or turnover and cannot rectify an apparent insufficiency by participating in the other auditor's work, as is the case in paragraph 5 below.
4. There may be circumstances where the group auditor is put in a temporary situation where the group auditor and related auditors directly perform work on less than approximately 50%, or the percentage considered appropriate in the circumstances, of the group assets, liabilities, cash flows, profit or turnover. For example, because of an acquisition made during the year, the percentage of work directly performed by the

group auditor and related auditors on the group assets changed from approximately 50% to approximately 30%. In such circumstances, when it is impractical for the group auditor to quickly react to the situation by either resigning as group auditor or being engaged to directly perform work on additional components, the group auditor may still continue to serve as group auditor for the current year. However, the group auditor attempts to increase the portion on which the group auditor and related auditors directly perform as soon as possible, or ordinarily does not continue the engagement in the following year.

5. **The group auditor should not accept or continue an engagement where the work on the financial information of a component that has been identified at group level as likely to include significant risks of material misstatement of the group financial statements is performed by an other auditor, unless the group auditor or a related auditor will be able to participate in the work of the other auditor.**
6. The group auditor considers the practicality of the group auditor or a related auditor participating in the work of the other auditor. For example, in the case of a component operating in a foreign jurisdiction, or in the case of a tight timetable for completing the audit, the group auditor may not be able to directly perform work on the component's financial information. **Where the group auditor or a related auditor is unable to participate in the other auditor's work, the group auditor should not accept or continue the engagement.**
7. **The group auditor should communicate to those charged with governance of the group:**
 - a. **The portion of group assets, liabilities, cash flows, profit or turnover on which the group auditor and related auditors will directly perform work and the portion on which other auditors will directly perform work, and**
 - b. **The group auditor's proposed participation in the work of other auditors where other auditors will perform the work on components that have been identified at group level as likely to include significant risks of material misstatement.**

The group auditor also makes those charged with governance of the group aware of any temporary situation in which the group auditor and related auditors do not directly perform work on a significant portion of the group assets, liabilities, cash flows, profit or turnover.

- (b) To facilitate the group auditor's and related auditors' participation in the work of other auditors, the following new requirement should be inserted in the ISA: **The other auditor, knowing the context in which the group auditor will utilize the other auditor's work, should cooperate with the group auditor.** (This is a requirement in extant ISA 600, "Using the Work of Another Auditor;" however, in finalizing the exposure draft, the task force and IAASB agreed not to retain the requirement as they

were of the view that the ISA deals with the group auditor's responsibilities and therefore should not contain a requirement for other auditors.)

- (c) The research referred to in paragraph 20 above should include research with regard to the 50% acceptance/retention proposal.

IAASB Action: Does the IAASB agree with the task force's recommended disposition?

ISA vs. IAPS

- 30. 16 respondents commented on the "split" between the ISA and the IAPS, and the detail of guidance provided. Six respondents were comfortable with the approach adopted to embed the key principles in the ISA, while providing more detailed guidance on the application of the ISAs to group audits in the IAPS. It was noted that this approach supports the philosophy that the standards and guidance in the ISAs apply to all audits. The IAPS achieves the objective of providing relevant guidance on the application of the standards to group audits.
- 31. Two respondents were of the view that the IAPS is too long and detailed, and that it should be changed to focus on areas in which additional guidance for the audit of group financial statements are needed specifically.
- 32. Eight respondents were of the view that the ISA, and in particular the group auditor's procedures, should be strengthened by moving guidance from the IAPS to the ISA (see Sole vs. Divided Responsibility section above). Recommendations included the guidance on acceptance and continuance as group auditor (see paragraph 29 above); the group auditor's risk assessment procedures, including determining the scope of work to be performed on the components' financial information (with a clear link to the audit risk standards); the procedures that the group auditor performs in relation to the related/other auditors work; and communication with those charged with governance (see paragraph 29.(a).7.)
- 33. One respondent was of the view that the ISA should deal with the group auditor's use of the work of other auditors in general, and that the IAPS should deal with the audit of entities having components.

Task Force Deliberations and Recommended Disposition

- 34. The task force reviewed the comments received on the ISA vs. IAPS. These comments were considered in conjunction with the comments received on sole vs. divided responsibility, in particular the requests to strengthen the group auditor's procedures (see Sole vs. Divided Responsibility section above), and the comments received on acceptance and continuance, in particular the requests for the group auditor or related auditor to participate in the work of an other auditor where the component has been identified at group level as likely to give rise to significant risks of material misstatement of the group financial statements (see paragraph 29.(a).5.).
- 35. The task force recommends that:

- (a) The ISA should be revised to include standards and guidance that are based on the guidance in the IAPS. Proposed wording for the standards and guidance to be included in the ISA is set out below. The task force acknowledges that it should give further consideration to the wording and that it may require amendment when read in the context of the other standards and guidance in the ISA. As a result, the IAASB is requested to consider the principles, rather than the exact wording.
1. **For components that are of individual financial significance or components that have been identified at group level as likely to include significant risks of material misstatement of the group financial statements, the group auditor should obtain an understanding of the components and their environments. In this regard, the group auditor or related auditors should direct inquiries to component management. Where the work on the financial information of these components will be performed by other auditors, the group auditor or related auditors should discuss with the other auditors, or key members of their teams, the susceptibility of the components to material misstatement of the financial information due to fraud or error. (IAPS.45 and IAPS.46)**
 2. **Where the work on the financial information of components that are of individual financial significance or components that have been identified at group level as likely to include significant risks of material misstatement of the group financial statements will be performed by other auditors, the group auditor or related auditors should participate in the other auditors' risk assessment procedures. (IAPS.46)** Where the work on the financial information of these components will be performed by related auditors, and the related auditors do not apply the same audit methodology as the group auditor, the group auditor ordinarily participates in the risk assessment procedures of the related auditors. (New)
 3. Where the work on the financial information of components that are of individual financial significance or components that have been identified at group level as likely to include significant risks of material misstatement of the group financial statements will be performed by related auditors or other auditors, the group auditor communicates to the related auditors or other auditors the results of the risk assessment procedures performed at group level that are relevant to the work of the related auditors or other auditors, including identified fraud risks. The group auditor requests the related auditors or other auditors to inform the group auditor if information comes to their attention that differs significantly from the information on which the group auditor's risk assessment was based. (IAPS.52) The nature, timing and extent of the communications are a matter for professional judgment and are affected by the group auditor's participation in the risk assessment procedures of the related auditors and other auditors. (New)
 4. **Where the work on the financial information of components that, based on the risk assessment procedures, have been identified as including significant risks of material misstatement of the group financial statements is performed by other auditors, the group auditor or related auditors should participate in the further**

audit procedures to be performed by the other auditors in response to the identified significant risks. (IAPS.62) The nature, timing and extent of the group auditor's or related auditors' participation in the other auditors' procedures is based on professional judgment and will be affected by the group auditor's assessment of the procedures performed in paragraphs 1 and 2 above.

5. **Where the work on the financial information of components that are of individual financial significance or components that have been identified at group level as likely to include significant risks of material misstatement of the group financial statements was performed by other auditors, the group auditor or related auditors should review the other auditors' working papers.** The extent of the reviews is based on professional judgment and is affected by the group auditor's assessment of the procedures performed in paragraphs 1, 2 and 4 above. The group auditor or related auditors focus the reviews on the working papers relevant to the significant risks of material misstatement of the group financial statements. (IAPS.62 and ISA 600.27) Where the work on the financial information of these components will be performed by related auditors, and the related auditors do not apply the same audit methodology as the group auditor, the group auditor ordinarily reviews the work of the related auditors. (New)
6. **Where the work on the financial information of components that, when aggregated with other individually insignificant components, are of financial significance or are likely to give rise to significant risks of material misstatement of the group financial statements was performed by other auditors, the group auditor should obtain the other auditors' evaluation of misstatements, and read the other auditors' reports.** (New) In order for the group auditor to obtain sufficient appropriate audit evidence to be able to express an audit opinion on the group financial statements, it may be necessary for the group auditor or related auditors to directly perform work on the financial information of these components or to participate in the work of the other auditors. The group auditor applies professional judgment in determining the nature, timing and extent of such procedures, which may include one or more of the following:
 - Meet with component management.
 - Perform planning and risk assessment procedures. These may be performed with the other auditors, or directly by the group auditor.
 - Perform further audit procedures in response to identified significant risks. These may be performed with the other auditors, or directly by the group auditor.
 - Participate in the other auditors' evaluation of audit evidence.
 - Participate in the closing and other key meetings between the other auditors and component management.
 - Review the other auditor's working papers. (New)

7. As discussed above, the nature, timing and extent of the group auditor's procedures are based on professional judgment, that is:

- The smaller the portion of group assets, liabilities, cash flows, profit or turnover that the group auditor and related auditors directly perform work on, or
- The greater the individual financial significance of the component or the significance of the risks of material misstatement of the group financial statements, or
- The lower the level of the group auditor's satisfaction with the professional qualifications, professional competence, and resources of the other auditor, or with the quality control processes of the other auditor's firm

The greater is the extent of work directly performed by the group auditor or related auditor, or the group auditor's or related auditor's participation in the other auditor's work. (IAPS.64)

- (b) Guidance on when to use a related auditor to perform procedures in relation to an other auditor and the related communications between the group auditor and the related auditor should be developed and inserted in the ISA.

IAASB Action: Does the IAASB agree with the task force's recommended disposition?

Re-exposure and Consultation

36. The task force is of the opinion that, should the IAASB agree with the recommended dispositions in this paper (which includes (a) tightening the definition of related auditors, (b) requiring the same work effort for sole and divided responsibility, and (c) revising guidance from the IAPS and including it as bold lettered obligations in the ISA), it will be necessary to re-expose the revised proposed ISA and IAPS.

IAASB Action: The IAASB is asked to consider whether the revised proposed ISA and IAPS should be re-exposed.

37. The task force discussed the possibility of a public hearing to further debate the issue of sole vs. divided responsibility. The task force is of the opinion that, at present, it is rather unlikely that the issue will be resolved by a public hearing, as participants may merely confirm their written comments. Furthermore, it would be difficult to hold only one public hearing in either Europe or North America, as these countries have split views on the issue. The task force may propose that a public hearing be held in the future.

IAASB Action: In the light of the recommended dispositions, and taking into account the proposal to re-expose the revised proposed ISA and IAPS, what is the IAASB view on holding a public hearing?

Project Timetable

38. The following revised timetable is proposed for the project:

IF NO RE-EXPOSURE	IF RE-EXPOSED	ACTION
June 2004	June 2004	<ul style="list-style-type: none"> Review summary of significant comments and the task force's recommended dispositions
December 2004	December 2004	<ul style="list-style-type: none"> Full review of comments and the task force's recommended dispositions Review of a first draft of the revised ISA and IAPS
March 2005	March 2005	<ul style="list-style-type: none"> Approval of the ISA and IAPS / Approval of the revised proposed ISA and IAPS, i.e. for re-exposure
	September 2005	<ul style="list-style-type: none"> Review of summary of significant comments and task force's recommended dispositions
	December 2005	<ul style="list-style-type: none"> Full review of comments and the task force's recommended dispositions Review of a first draft of the revised ISA and IAPS
	March 2006	<ul style="list-style-type: none"> Approval of the ISA and IAPS – Effective date January 1, 2007

39. The task force is mindful of the importance of this project and the urgency of its completion. As a result, the task force has considered the following accelerated timetable for re-exposure, but is concerned that the significance of the comments received and those that may be received on re-exposure, may make it difficult to give them due consideration in a shorter period of time.

IF RE-EXPOSED	ACTION
June 2004	<ul style="list-style-type: none"> Review summary of significant comments and the task force's recommended dispositions
September 2004	<ul style="list-style-type: none"> Full review of comments and the task force's recommended dispositions Review of a first draft of the revised ISA and IAPS
December 2004	<ul style="list-style-type: none"> Approval of the revised proposed ISA and IAPS, i.e. for re-exposure
June 2005	<ul style="list-style-type: none"> Review of summary of significant comments and task force's recommended dispositions
September 2005	<ul style="list-style-type: none"> Full review of comments and the task force's recommended dispositions Review of a first draft of the revised ISA and IAPS
December 2005	<ul style="list-style-type: none"> Approval of the ISA and IAPS – Effective date June 1, 2006

IAASB Action: The IAASB is asked to consider the proposed timetables (including the accelerated timetable) and to advise the task force accordingly.

Appendix 1

List of Respondents

IFAC Member Bodies

1.	American Institute of Certified Public Accountants (AICPA) <i>United States</i>
2.	Association of Chartered Certified Accountants (ACCA) <i>United Kingdom</i>
3.	Canadian Institute of Chartered Accountants (CICA) <i>Canada</i>
4.	Certified General Accountants Association of Canada (CGA Canada) <i>Canada</i>
5.	Chinese Institute of Certified Public Accountants (CICPA) <i>China</i>
6.	Compagnie Nationale des Commissaires aux Comptes (CNCC) & Conseil Supérieur de l'Ordre des Experts-Comptables (OEC) <i>France</i>
7.	Den norske Revisorforening (DnR) <i>Norway</i>
8.	Foreningen af Statsautoriserede Revisorer (FSR) <i>Denmark</i>
9.	Föreningen Auktoriserade Revisorer (FAR) <i>Sweden</i>
10.	Hong Kong Society of Accountants (HKSA) <i>Hong Kong</i>
11.	Institut der Wirtschaftsprüfer (IDW) <i>Germany</i>
12.	Institut des Reviseurs d'Entreprises (IRE) Belgium <i>Belgium</i>
13.	Institute of Certified Public Accountants of Kenya <i>Kenya</i>
14.	Institute of Chartered Accountants in England and Wales (ICAEW) <i>United Kingdom</i>
15.	Institute of Chartered Accountants in Ireland (ICAI) - Auditing Standards Committee <i>Ireland</i>
16.	Institute of Chartered Accountants of New Zealand (ICANZ) <i>New Zealand</i>
17.	Institute of Chartered Accountants of Pakistan (ICAP) <i>Pakistan</i>
18.	Institute of Chartered Accountants of Scotland (ICAS) <i>United Kingdom</i>
19.	Japanese Institute of Certified Public Accountants (JICPA)

	Japan
20.	Koninklijk Nederlands Instituut van Registeraccountants (Royal NIVRA) <i>The Netherlands</i>
21.	Malaysian Institute of Accountants (MIA) & Malaysian Institute of Certified Public Accountants (MICPA) <i>United Kingdom</i>
22.	South African Institute of Chartered Accountants (SAICA) & Public Accountants' & Auditors' Board (PAAB) <i>South Africa</i>

Firms

1.	Deloitte Touche Tohmatsu (DTT) <i>United States</i>
2.	Ernst & Young <i>United Kingdom</i>
3.	Grant Thornton <i>United States</i>
4.	KPMG <i>Canada</i>
5.	Mazars <i>United Kingdom</i>
6.	Moore Stephens <i>United Kingdom</i>
7.	PricewaterhouseCoopers (PwC) <i>United Kingdom</i>

Others

1.	Auditing Practices Board (APB) <i>United Kingdom</i>
2.	Australasian Council of Auditors-General (ACA-G) <i>Australia</i>
3.	Australian Auditing & Assurance Standards Board (AuASB) <i>Australia</i>
4.	Basel Committee on Banking Supervision <i>Switzerland</i>
5.	Fédération des Experts Comptables Européens (FEE) <i>Belgium</i>
6.	German Certified Public Accountants Society e.V. (GCPAS) <i>Germany</i>
7.	International Organization of Securities Commissions (IOSCO) <i>United States</i>
8.	London Society of Chartered Accountants (LSCA) <i>United Kingdom</i>
9.	New York State Society of Certified Public Accountants (NYSSCPA) <i>United States</i>

10. [Ramachandran Mahadevan](#)

India

11. [Richard Regal](#)

United States

Appendix 2

Arguments Against and Supporting Divided Responsibility

ARGUMENTS AGAINST DIVIDED RESPONSIBILITY

Arguments against divided responsibility, and the way it was provided for in the proposed revised ISA 600, included the following:

- In the current climate, in the wake of accounting scandals stretching back over the last twenty years, and in view of the well-documented problems associated with the audit of complex business empires that are designed to be opaque, it seems clear that divided responsibility increases the risk that major frauds will go undetected and sends out the wrong messages about accountability within the profession.
- The European Commission has already highlighted via the draft revised 8th Company Law Directive that, post-Parmalat, sole responsibility by group auditors will be expected.
- There is no justification for allowing a national standard setter to override what is required for compliance with ISAs. If the IAASB believes that divided responsibility is acceptable then it should allow divided responsibility in all cases and should note that some jurisdictions restrict auditors' ability to divided responsibility.
- It is not appropriate for ISAs to refer to national standards because doing so undermines the credibility and the objective of international standards. The objective of ISAs is to establish audit requirements that auditors, at a minimum, should comply with. It may be appropriate for national standards to introduce additional or more stringent requirements than those required in an ISA. In this circumstance, compliance with national standards will ensure compliance with ISAs. An unqualified reference to national standards within an ISA will result in inconsistent and potentially lower quality audit practices and, at the same time, allow auditors to state they have complied with ISAs.
- Most jurisdictions do not permit divided responsibility; those that do, do not mandate it, and auditors therefore have a choice. If the revised ISA 600 were to require sole responsibility there would be no direct conflict with those jurisdictions that permit divided responsibility.
- Users of financial statements are critical of inconsistent audit quality. The retention of divided responsibility serves to perpetuate the potential for variation in the audit standards that are applied to the components of the group. Sole responsibility provides the users of financial statements with certainty of the identity of the auditor responsible and the standards that he has applied in undertaking the audit of the group financial statements; this key information is specified in the auditor's report.
- The standards based on the new audit risk model require the group auditor to obtain an understanding of the [group] and its environment sufficient to design and perform further audit procedures. The group auditor is required to make risk assessments at the [group] financial statement and assertion levels and to design and perform audit procedures in response to those risks. The standards allow the performance of audit procedures to be delegated to others but they in no way allow the responsibility for their performance to be delegated. Whatever arguments there may have been for permitting divided responsibility

under the previous risk model there does not seem to be any justification for its retention under the new audit risk model.

- An argument cited in support of divided responsibility is that it avoids duplication of work. However, as the proposed revised ISA 600 and the IAPS explain, accepting sole responsibility for the group audit opinion does not mean that the group auditor cannot use the work of another auditor. Undoubtedly, the group auditor must perform sufficient procedures to satisfy himself regarding the professional qualifications, competence, independence and quality control processes of the other auditor and, having done so, must then determine the procedures the group auditor believes are necessary in order to be satisfied that the work performed by the other auditor provides sufficient appropriate audit evidence in the context of the audit of the group financial statements.
- Those who advocate divided responsibility often cite transparency as one of the benefits. However, if the group auditor has obtained sufficient appropriate evidence to support the opinion on the group financial statements, a reference to other auditors may confuse more than it clarifies. In addition, the proposed guidance on divided responsibility in the proposed revised ISA 600 recommends that the auditor's report indicate only the magnitude of the portion of the group financial statements audited by other auditors and makes no reference to the need to identify the other auditors. This does not seem to be significantly more transparent.
- The users of the auditor's report need to understand who is ultimately responsible for the auditor's opinion on the group financial statements.
- The interaction of the revised ISA 600 with proposed PCAOB requirements relating to the retention of audit files at the office of group auditors with sole responsibility may result in an increase of instances in which responsibility is divided (to avoid PCAOB requirements). This outcome is considered to be highly undesirable.
- The International Accounting Standards Committee (IASC), as it then was, achieved real credibility as a standard setter only when it abandoned its practice of allowed alternative treatments. As the IASC found, allowed alternatives do not help the process of convergence, they hinder it. The IAASB should find it easier to remove this allowed alternative than the IASC did for some of its alternatives. The IASC had to ask countries to adopt treatments that they had previously prohibited or that ran counter to current practice. This would not be the case if the IAASB decided not to allow divided responsibility. In the context of financial reporting standards, the problems of allowed alternative treatments can be mollified by disclosure, particularly disclosure of the effects of the chosen treatment. This is not possible for auditing standards as there is no mechanism for the auditor to calculate, far less disclose, the effect of using different audit methods.

ARGUMENTS SUPPORTING DIVIDED RESPONSIBILITY

Arguments supporting divided responsibility included the following:

- In the situation where the group auditor has used the work of another auditor, but decides not to assume responsibility for that work, it is important for the users of financial statements to understand that a significant part of the audit was completed by another auditor.

- Eliminating divided responsibility may reduce the ability of small and medium sized audit firms to participate in national and international audits. For example, a small audit firm (the “group auditor”) may audit a company that has a subsidiary in another location. It may not be practicable for the group auditor to perform the audit of the subsidiary, so another audit firm audits the subsidiary and issues a report. The group auditor uses the work of the other auditor and determines that it is appropriate to refer to the other auditor’s work in the group auditor’s report. Removing the ability of small and medium sized audit firms to refer to the work of the other auditor may promote the transference of work by multi-location or multi-jurisdiction entities to the large auditing firms, effectively cutting out the small and medium sized audit firms from certain engagements.
- There are certain circumstances where it is almost impossible for a group auditor to avoid using the work of the other auditor, for example in the case of an equity investee. The equity investee appoints its own auditor. The group auditor may not be able to obtain sufficient access to the other auditor or to the equity investee to be able to allow the group auditor to take sole responsibility for the group financial statements. In that case the auditor may have no choice but to use the work of the other auditor or be faced with having to make a decision to disclaim an opinion due to a scope limitation. Alternatively, the investor entity may be forced to change auditors to align with the auditor used by the equity investee to avoid an unfavorable opinion. In some cases, for example, joint ventures with multiple investors, there may be a number of auditors for the investor entity other than the auditor for the equity investee.
- In some situations, it may be impracticable for the group auditor to review the other auditor’s work or to use other procedures which would be necessary to satisfy the group auditor as to the audit performed by the other auditor. This may be the case, for example, where the other auditor prepares working papers in a language other than that used by the group auditor, and where the entity’s documents cannot be readily understood by the group auditor for language or other reasons.
- If the group auditor is not permitted to refer to the other auditor’s report it may lead to the entire audit of a component essentially being re-performed. The component would incur additional costs, in terms of both the monetary cost of the additional procedures and the personnel time taken to satisfy the group auditor’s requirements.