

## INTERNATIONAL STANDARD ON AUDITING 550 (REVISED)

### RELATED PARTIES

(Effective for audits of financial statements for periods commencing on or after [    ])

### CONTENTS

	Paragraph
Introduction .....	1- <del>56</del>
Definitions .....	<del>67-78</del>
Responsibilities of Management and Those Charged with Governance .....	<del>89-940</del>
<del>Initial Discussion Among the Engagement Team</del> <del>Planning the Audit</del> .....	<del>101-</del>
<del>123</del>	
<del>Communication Within the Engagement Team</del> .....	<del>14-15</del>
Risk Assessment Procedures .....	<del>136-</del>
<del>302</del>	
<del>Inquiries of Management and Others Within the Entity</del> .....	<del>14-16</del>
Understanding the <del>Ownership and Control of the Entity's and its</del> Relationships <del>with its with</del> <del>its Components Related</del> and Other Parties .....	<del>178-</del>
<del>224</del>	
Management's Identification and Disclosure of Related Party Relationships and Transactions .....	<del>235-</del>
<del>279</del>	
Identification of Related Party Risk Factors .....	<del>2830-</del>
<del>2934</del>	
Consideration of Other Information Obtained .....	<del>302</del>
<del>Assessment of the Significant</del> Risks <del>of Material Misstatement</del> Due to Related Parties .....	<del>313-346</del>
<del>Non-Arm's Length</del> Transactions <del>Giving Rise to as</del> Significant Risks <del>Due to Related Parties</del> .....	<del>335-</del>
<del>346</del>	
<del>Communication Within the Engagement Team</del> .....	<del>35-36</del>
Responses to the Risks of Material Misstatement Due to Related Parties .....	<del>37-465</del>
Consideration of Materiality in Responding to Assessed Risks .....	38
Testing the Operating Effectiveness of Internal Control .....	39-41
Substantive Procedures Responsive to Assessed Risks .....	<del>42-465</del>
Responses to Significant Risks .....	<del>476-523</del>

Substantive Procedures to Respond to Significant Risks.....	487-
523	
Identification of Previously Undisclosed Related Party Relationships or Transactions.....	534-56
<u>Measurement Considerations .....</u>	<u>54-55</u>
Disclosures Asserting Related Party Transactions to be at Arm’s Length .....	567-612
Communications with Those Charged with Governance.....	623-635
Written Representations .....	646-67
Evaluation of Related Party Disclosures and Reporting .....	68-76
<u>Expressing Rendering an Opinion on the Fair Presentation of the Financial Statements Prepared in Accordance with a Financial Reporting Framework Designed to Achieve Fair Presentation .....</u>	<u>68-72</u>
<u>Expressing Rendering an Opinion Whether the on Financial Statements Prepared in Accordance with a Comply with the Applicable Financial Reporting Framework not Designed to Achieve Fair Presentation.....</u>	<u>73-76</u>
<u>Inability to Obtain Sufficient Appropriate Audit Evidence Regarding Related Party Disclosures .....</u>	<u>77</u>
Effective Date.....	787

International Standard on Auditing (ISA) 550 (Revised), “Related Parties,” 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 ISAs.

## Introduction

1. The purpose of this International Standard on Auditing (ISA) is to establish ~~basic principles and essential procedures~~standards for, and provide guidance on, the auditor's responsibilities and audit procedures regarding related parties, and transactions with such parties, when performing an audit of financial statements. These ~~basic principles, essential procedures, standards~~ and guidance may also be relevant for audits of historical financial information other than financial statements.
- ~~2. Ordinarily, disclosure requirements for related party relationships and transactions are set out in the applicable financial reporting framework, including law and regulation. This ISA does not apply when:~~
  - ~~(a) The applicable financial reporting framework does not establish related party disclosure requirements; and~~
  - ~~(b) The auditor is only required to report whether the financial statements have been prepared, in all material respects, in accordance with the applicable financial reporting framework.~~
2. An entity may enter into related party transactions as part of its normal business. Because these transactions may not be conducted at arm's length, financial reporting frameworks ordinarily require them to be disclosed, so that users of financial statements can understand the nature of the transactions and their financial effects. Financial reporting frameworks may also require disclosure of related party relationships to enable users to understand the nature of the relationships and their potential effects on the financial statements.
3. **The auditor should**~~In planning and performing the audit to obtain sufficient appropriate audit evidence regarding the identification and disclosure of related party relationships and transactions, and their effects on the financial statements~~reduce audit risk to an acceptably low level, the auditor should assess and respond to the risks of material misstatements in the financial statements due to related parties in the context of the entity's applicable financial reporting framework.
- ~~4. An entity may enter into related party transactions as part of its normal business. Because these transactions may not be conducted at arm's length, financial reporting frameworks ordinarily require them to be disclosed, so that users of financial statements can understand the nature of the transactions and their financial effects. Financial reporting frameworks may also require disclosure of related party relationships to enable users to understand the nature of the relationships and their potential effects on the financial statements.~~
- ~~54.~~ The risk that the entity may not identify and appropriately disclose related party relationships and transactions may be high for a number of reasons, including the following:
  - (a) Related parties may operate through an extensive and complex range of relationships and structures, and may enter into complex transactions;
  - (b) Information systems may not be designed to distinguish or summarize transactions and outstanding balances between an entity and its related parties;
  - (c) Not all related party transactions may be conducted with an exchange of consideration;

- (d) Related party transactions may not be conducted in the normal course of business; and
- (e) Transactions with related parties may be controlled, manipulated, or concealed by management for fraudulent or other purposes.

~~65. For these reasons, T~~here is, ~~therefore~~, an inherent level of uncertainty associated with financial statement assertions regarding complete related party identification and disclosure. ~~Because of this, the risk of not identifying a material misstatement in the financial statements due to related parties often may be higher than the risk of not identifying material misstatements in other financial statement assertions.~~ Nevertheless, the auditor plans and performs the audit to have a reasonable expectation of identifying all material related party relationships and transactions.

## Definitions

~~76.~~ This ISA ~~refers to~~ adopts the definitions ~~regarding related parties~~ in IAS 24<sup>1</sup> regarding related parties to assist the auditor ~~to in~~ understanding the requirements and guidance ~~in this of the~~ ISA. If the applicable financial reporting framework provides different related party definitions, the auditor ~~refers to~~ uses those definitions for the purpose of the audit.

~~87.~~ In this ISA:

- (a) “Arm’s length transaction” means a transaction conducted on such terms and conditions as between a willing buyer and a willing seller acting as if they were unrelated and pursuing their own best interests~~;-~~;
- (b) “Conflict of interest” means, in relation to management or those charged with governance, a situation that arises from (i) their being in a position to advance their own personal interests contrary to their fiduciary responsibilities towards the entity, or (ii) having responsibilities to two or more entities that are conflicting;
- (cb) “Horizontal group” means a group of entities that are related through common control or significant influence but that falls outside the requirements for consolidation under the applicable financial reporting framework;
- (ed) “Material misstatement due to related parties” means a material misstatement of the financial statements arising from:
  - (i) The ~~omission of non~~-disclosure of related party relationships or transactions that is required by the applicable financial reporting framework, or is otherwise needed ~~to avoid the presentation of misleading financial statements for fair presentation of the financial statements when the financial reporting framework is designed to achieve fair presentation~~;
  - (ii) The incomplete, unclear or misleading disclosure or presentation of such relationships or transactions; or
  - (iii) Other financial effects of these relationships or transactions, including fraud~~;-~~;

<sup>1</sup> See Appendix 1.

- (~~ed~~) “Related party risk factors” means events or conditions affecting the entity that indicate an increased risk that undisclosed related party relationships or transactions exist; and
- (~~fe~~) References to disclosure of related party transactions include disclosure of related party balances where ~~ren~~ required by the applicable financial reporting framework.

### **Responsibilities of Management and Those Charged with Governance**

~~98~~. Management is responsible for identifying and disclosing related party relationships and transactions in accordance with the applicable financial reporting framework. This responsibility requires management to design and implement adequate controls to achieve such an objective.

~~109~~. Those charged with governance are responsible for monitoring how management has discharged its responsibilities for identifying and disclosing related party relationships and transactions in accordance with the applicable financial reporting framework. In carrying out that responsibility, those charged with governance need to understand the nature and business purposes of the related party relationships and transactions, and their effects on the financial statements.

### **Planning the AuditInitial Discussion Among the Engagement Team**

~~104~~. During As part of the initial planning of the audit discussion among the engagement team required by ISA 315, “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement,” members of the ~~engagement~~ team should discuss:

- (a) The nature and extent of the entity’s ~~known~~ related party relationships and transactions; and
- (b) The C~~ircumstances~~ or conditions of the entity that may indicate the existence of undisclosed related party relationships or transactions.

~~112~~. This discussion, ordinarily among key members of the engagement team, provides an opportunity for the more experienced team members to share their insights regarding how the financial statements are, or may be, ~~influenced~~ affected by related party relationships and transactions. The discussion is based on knowledge gained from previous audits and from audit procedures performed during the client acceptance and continuance process. For an initial engagement, the discussion may also be based on information obtained from communicating with previous auditors. Paragraph 17 of ISA 315, “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement,” addresses relevant factors to consider in planning the discussion.

~~123~~. Matters that are ordinarily discussed include:

- The importance that management and those charged with governance attach to the identification and disclosure of related party relationships and transactions.;
- The importance of remaining alert during the audit to the potential for material misstatement due to related parties.;

- The ways in which members of the engagement team believe the financial statements may be at risk of material misstatement due to related parties, and how management could perpetrate and conceal fraud through related party mechanisms.;
- The related party implications of the entity's organizational structure and business, such as complex capital structures or ownership issues, and extensive transactions with offshore entities.
- The audit procedures that might assist to assess and respond to the risks of material misstatement due to related parties, and whether certain types of audit procedures are would be more effective than others.;
- The risk of management override of relevant controls.

### **Communication Within the Engagement Team**

#### **~~14. The auditor should communicate to all members of the engagement team:~~**

- ~~(a) The name of each known related party before the audit starts; and~~
- ~~(b) The name of any related party identified during the audit on a timely basis.~~

~~15. Continued communication within the engagement team of information that may affect the assessment of the risks of material misstatement due to related parties, is important throughout the audit. Engagement team members undertake to communicate the names of newly identified related parties to the rest of the engagement team on a timely basis.~~

### **Risk Assessment Procedures**

~~16. ISA 315 requires the auditor to obtain an understanding of the entity and its environment, including its internal control, sufficient to identify and assess the risks of material misstatement of the financial statements due to fraud or error. The auditor obtains this understanding by performing risk assessment procedures, which calls for gathering, updating and analyzing information throughout the audit.~~

#### **137. To identify the risks of material misstatement due to related partiesAs part of the risk assessment procedures required by ISA 315, the auditor should:**

- (a) Inquire of management and others within the entity regarding the identities of related parties;
- (ba) Obtain an understanding of the ownership of the entity and the way in which it the entity's is controlled, and the nature, extent, and substance of its relationships with its components related and other parties;
- (cb) Obtain an understanding of how management identifies and discloses related party relationships and transactions;
- (de) Consider whether one or more related party risk factors are present (see paragraphs 30 and 31); and

- (e~~d~~) Consider whether other information obtained indicates risks of material misstatement due to related parties.**

*Inquiries of Management and Others Within the Entity*

14. The auditor obtains, through inquiries of management and others within the entity, a complete and up-to-date list of related parties to assist in the performance of risk assessment and further audit procedures. For a recurring audit, the auditor's inquiries may be limited to updating the auditor's knowledge of the related parties gained from previous audits.

15. Regardless of whether they are considered part of management, the auditor inquires of the following persons within the entity regarding related parties:

- (a) Those charged with governance;
- (b) Personnel who initiate, process or record significant and unusual transactions, and those who supervise or monitor such personnel;
- (c) Internal audit;
- (d) In-house legal counsel; and
- (e) The chief ethics officer or equivalent person.

In addition, the auditor may inquire of other personnel considered appropriate.

16. The auditor may also identify related parties through the performance of other audit procedures, including:

- Reviewing significant investment transactions during the period.
- Reviewing shareholder records containing the names of the principal shareholders.
- Reviewing minutes of the meetings of shareholders and those charged with governance, and other relevant statutory records.
- Where appropriate, inquiring of previous auditors regarding the identities of related parties.

*Understanding ~~the Ownership and Control of the Entity's and its~~ Relationships with its ~~Components Related~~ and Other Parties*

17. In obtaining an understanding of the entity's relationships with its related and other parties, the auditor considers the nature, extent and substance of:

- (a) The entity's relationships with related parties that have been identified;
- (b) The relationships between the entity's principal owners and parties that may be related to them; and
- (c) The entity's relationships with special-purpose entities.

18. ~~ISA 315 requires the auditor to obtain an understanding of the nature of the entity. This involves:~~  
~~In considering the nature and extent of the entity's identified related party relationships, the auditor~~

- (a) ~~Understanding the ownership of the entity;~~

~~(b) Determining~~ how the entity is controlled or significantly influenced, ~~and~~

~~(c) Considering whether the entity has entered into significant transactions with persons or entities that might have a relationship with the entity's principal owners,<sup>2</sup> and how it controls or significantly influences other parties. The exercise of control or significant influence may occur indirectly through intermediate parties. Control may also be exercised jointly with other parties. Control or significant influence can ordinarily be recognized by considering a party's ownership interests in, or extent of voting power over, an entity. In other cases, the operation of effective control or significant influence may not be readily apparent for reasons such as:~~

- ~~• A complex shareholding structure;~~
- ~~• The location of shareholder or other relevant records in a foreign or offshore jurisdiction; or~~
- ~~• Control or significant influence over management or those charged with governance by external parties.~~

~~19. Understanding the substance of the entity's identified related party relationships is relevant in evaluating the effects of the relationships on the financial statements. For example, the entity may have control over a transfer pricing arrangement with a related party. An understanding of the substance of the relationship and of the transfer pricing arrangement is necessary for the auditor to evaluate the related financial effects (including risks and contingencies) and their disclosure in the financial statements, especially where the related party is not consolidated.~~

~~1920. It is also appropriate to Cconsidering the nature, extent and substance of the potential relationships is particularly appropriate when that the entity's principal owners might have with parties that may be related to them, as financial reporting frameworks often define parties to be related if they are under common control. Further, it is appropriate to consider whether the principal owners exercise dominant influence over the entity. When dominant influence exists, there is a In such circumstances, the higher risk of the owners of overriding controls is higher, because the principal owners may, through direct or indirect control or significant influence, lead to cause the entity to enter into non-arm's length transactions with persons or entities other parties related to them. A Hhorizontal groups<sup>3</sup> represents one particular class of entities in which such type of structure where an understanding of the relationships exist among the various parties within the group is important. These relationships within such a group may be difficult to identify completely because such as the groups falls outside the requirements for consolidation under the applicable financial reporting framework.~~

~~20. The auditor obtains an understanding of the substance of the entity's relationships with its various components, and other parties with which it has entered into significant transactions, not just their legal forms. Such other parties include (a) non-consolidated entities such as partnerships, joint ventures and special-purpose entities, (b) major suppliers and customers, and (c) other parties with which the entity has entered into material contracts or agreements. It will often be clear that these relationships are designed to achieve objectives consistent with the nature of the entity's business. For example, the entity may outsource manufacturing of its products to a component~~

<sup>2</sup> Appendix 1 provides examples of definitions of control and significant influence.

<sup>3</sup> See illustrations in Appendix 2.



~~located in another country to take advantage of lower production costs. In other cases, unusual or unexpected business purposes may indicate the existence of related party risk factors in response to which further audit procedures may be appropriate.~~

21. The auditor needs to understand the nature and extent of the entity's relationships with special-purpose entities,<sup>4</sup> as these may act as vehicles for related party transactions. Such entities are ordinarily established for limited purposes, such as providing financing, liquidity, hedging or credit support. They may be in the form of corporations, partnerships, trusts, or other types of arrangements. In many cases, they do not have physical operating characteristics, which makes it relatively easier for them to be set up and dissolved. In addition, these entities tend not to be consolidated and often do not issue financial statements. For these reasons, it is important for the auditor to understand their substance and the purposes for which they have been set up as they may involve previously undisclosed related parties.

22. In identifying related party relationships not previously disclosed, the auditor may also consider the need to understand the nature and substance of the entity's relationships with:

- Its major suppliers and customers; and
- Other parties with which it has entered into significant contracts or agreements.

~~21. In understanding the nature of the entity in the context of related parties, the auditor uses a combination of prior experience with the entity and audit procedures performed for the period under audit.~~

~~22. The auditor should inquire of management, those charged with governance, internal audit and others within the entity, as appropriate, regarding the names of known related parties and the nature of relationships that management and those charged with governance have with other parties.~~

~~23. The auditor's inquiries of those charged with governance, internal audit and others within the entity, as appropriate, may encourage these individuals to disclose related party information to the auditor that may not otherwise have been communicated. The auditor exercises professional judgment in determining the persons within the entity to whom it is appropriate to direct inquiries, and the extent of such inquiries. Examples of others within the entity to whom the auditor may direct inquiries include:~~

- ~~• Operating personnel not directly involved in financial reporting;~~
- ~~• Employees who initiate, process or record complex or unusual transactions, and those who supervise or monitor such employees;~~
- ~~• In-house legal counsel; and~~
- ~~• The chief ethics officer or equivalent person.~~

~~24. Other procedures that the auditor may perform include:~~

<sup>4</sup> Special-purpose entities are sometimes referred to as structured finance entities.

- ~~Reviewing the effects of changes to the list of known related parties arising, for example, as a result of acquisitions and disposals, compared to that of the prior reporting period.~~
- ~~Reviewing shareholder records containing the names of the principal shareholders.~~
- ~~Reviewing minutes of the meetings of shareholders and those charged with governance, and other relevant statutory records.~~
- ~~Where appropriate, communicating with predecessor auditors regarding the names of known related parties.~~
- ~~Where appropriate, requesting other auditors currently involved in the audit to communicate the names of newly identified related parties and the types of transactions with such parties.~~

*Management's Identification and Disclosure of Related Party Relationships and Transactions*

~~235.~~ As required by ISA 315, the auditor obtains an understanding of the controls that management has designed and implemented. This understanding helps the auditor to (a) identify types of potential misstatements, (b) consider factors that may affect the risks of material misstatement, and (c) design the nature, timing and extent of further audit procedures.

~~26. Controls within some entities that address the identification and disclosure of related party relationships and transactions may be weak or non-existent. This may be due to a number of reasons, such as:~~

- ~~The low importance attached by management to related party identification and disclosures;~~
  - ~~An intentional disregard for such controls because related party disclosures may reveal information that management considers sensitive; or~~
  - ~~An insufficient understanding by management of the disclosure requirements of the financial reporting framework.~~
- ~~— The absence of adequate controls over related party transactions increases the risk that they will not be identified and appropriately disclosed. Paragraphs 42, 47 and 51 set out substantive audit procedures that respond to the assessed risks.~~

~~247.~~ Where the entity has ~~In the case of other entities with appropriate controls relating to related parties,~~ the auditor may decide to rely on them. In that case, if the auditor evaluates whether the controls ~~determines that they~~ have been properly designed and implemented, and have operated effectively throughout the period under audit. Examples of such controls include policies and procedures dealing with:

- The declaration and updating of the interests management and those charged with governance hold in related parties at appropriate times during the reporting period.
- The assignment of responsibilities within the entity for identifying, recording, and summarizing related party transactions.
- The communication of newly identified related parties to appropriate entity personnel so that transactions between the entity and such parties are properly recorded and disclosed.
- The review and approval by those charged with governance of related party transactions involving management.

- The specific assignment to an appropriate level of management of overall responsibility for reviewing the completeness, adequacy, and accuracy of related party disclosures prepared by other entity personnel.

258. Procedures the auditor may perform to obtain an understanding of the entity's controls addressing related parties include:

- (a) ~~• Inquiring of~~ ~~Discussing with~~ relevant entity personnel how they determine the completeness of disclosure of related party transactions.;
- (b) ~~•~~ Inquiring how management and those charged with governance declare and update their interests in related parties. The process they use may be systematic, involving confirmations at specific times during the reporting period, or it may be made a specific responsibility for them to report their interests to the entity.;
- (c) ~~•~~ Inquiring how management and those charged with governance approve related party transactions involving actual or perceived conflicts of interest.;
- (d) ~~•~~ Inquiring into the controls for monitoring disclosure.

269. In obtaining an understanding of the entity's controls, the auditor- also considers ~~the effect of~~ how the existence of related parties in which management is known to have control, significant influence, or financial or other interests, ~~on may affect~~ the potential for management to override controls to perpetrate fraud. As discussed in ISA 240, "The Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements," fraudulent financial reporting and misappropriation of assets often arise through management override of controls that otherwise appear to be operating effectively. The risk of management override of controls is greater if there are related party relationships involving management, because these relationships may present management with greater incentives and opportunities to perpetrate fraud. For example, management's financial interests in certain related parties may provide incentives for management to override controls to commit fraud by (a) directing the entity, against its interests, to conclude transactions benefiting the related parties, or (b) colluding with those parties or directing their actions. Examples of such fraud include:

- Creating fictitious terms of transactions with related parties designed to misrepresent the substance of these transactions.
- Authorizing the transfer of assets to related parties at amounts significantly below market value.
- Engaging in complex transactions with related parties that are structured to misrepresent the financial position or financial performance of the entity.

27. Controls within some entities that address the identification and disclosure of related party relationships and transactions may be weak or non-existent. This may be due to a number of reasons, such as:

- The low importance attached by management to related party identification and disclosure;
- The lack of appropriate oversight by those charged with governance;

- An intentional disregard for such controls because related party disclosures may reveal information that management considers sensitive; or
- An insufficient understanding by management of the disclosure requirements of the applicable financial reporting framework.

The absence of adequate controls over related party transactions increases the risk that they will not be identified and appropriately disclosed. Paragraphs 42 and 48 set out substantive requirements that respond to the assessed risks.

#### *Identification of Related Party Risk Factors*

2830. In obtaining an understanding of the entity and its environment, the auditor may identify related party risk factors. Examples of these factors include:

- A complex organizational or ownership structure that may mask the existence of undisclosed related parties and transactions with such parties.;
- Significant family relationships with, or business interests in, the entity or its components.
- ~~The existence of s~~Significant transactions outside the normal course of business that may indicate the potential involvement of related parties.;
- ~~The existence of i~~ncentive programs for management that may encourage earnings management or fraud through the use of related parties.

The auditor considers these risk factors in the risk assessment process.

2934. Although such risk factors may not necessarily indicate the existence of previously unidentified related party relationships or transactions, they have often been present in circumstances where such relationships or transactions have been identified in the past. The significance of related party risk factors varies. Some ~~of these factors will be present in entities where the specific conditions on which the risk factors are based do not may~~ present risks of material misstatement whereas others may not. Accordingly, the auditor exercises professional judgment in determining whether a related party risk factor is present, and whether it is to be considered in assessing the risks of material misstatement ~~of the financial statements~~ due to related parties. Appendix 3 presents other examples of related party risk factors that the auditor may consider in identifying risk.

#### *Consideration of Other Information Obtained*

302. The auditor also considers whether other information obtained about the entity and its environment indicates risks of material misstatement due to related parties. Other information that may be relevant includes information obtained from the auditor's client acceptance and retention processes, press reports about the entity, and experience gained on other engagements performed for the entity.

#### **Significant Assessment of the Risks of Material Misstatement Due to Related Parties**

313. ISA 315 requires the auditor to identify and assess the risks of material misstatement at the assertion level and to determine which of the identified risks, in the auditor's judgment, require special audit consideration. Such risks are described as "significant risks."

324. Using information gathered from the risk assessment procedures, the auditor should determine which conditions or events may indicate the existence of transactions giving rise to concerning related parties represent significant risks due to related parties that require special audit consideration.

*Non-Arms' Length Transactions Giving Rise to as Significant Risks Due to Related Parties*

335. ~~Related party transactions may form a routine part of an entity's operations. There may be little ambiguity regarding their terms and purposes if they are demonstrably undertaken on an arm's length basis. For example, the entity may, as part of its normal sourcing arrangements, purchase inventory for resale from a related party on fully disclosed terms and conditions that are consistent with those provided to arm's length parties. Significant transactions outside the normal course of business, or that otherwise appear unusual, ordinarily give rise to significant risks as they are non-routine, and therefore have greater inherent risks. For example, the entity may enter into significant transactions with certain parties on terms that are non-arm's length. As the nature and substance of the transactions may not be clear, they require special audit consideration and appropriate audit responses (see paragraphs 47-52).~~

34. ~~There may, however, also be some significant legitimate business reasons for the entity to enter into non-arm's length transactions with its related parties outside the normal course of business, or that otherwise appear unusual, that do not give rise to significant risks. This will be the case if (a) there is a legitimate business rationale for the entity to enter into these transactions; (b) the terms and conditions of the transactions are well documented and understood; and (c) the substance of the transactions is clear. , for e~~Examples of such transactions are:

- ~~, to s~~Supporting the start-up operations of a component related party through an interest-free loan. ~~These transactions may not represent significant risks if they are well documented and understood, and their terms and conditions are fully disclosed.~~
- Transferring receivables to a special-purpose entity to raise funds for an approved business purpose.

36. ~~In other circumstances, however, the entity may enter into non-arm's length transactions with certain parties so that its interests are subordinated to those of the other parties without apparent legitimate reason. For example, the entity may enter into a significant transaction on non-arm's length terms, with the result that it takes on risk that appears disproportionate to the potential rewards. Disclosure of such a transaction may be particularly sensitive to the other parties involved and, accordingly, evidence of the substance of the transaction may be limited. Such circumstances represent significant risks requiring special audit consideration.~~

**Communication Within the Engagement Team**

35. The auditor should communicate the outcome of the risk assessment procedures, including the names of all identified related parties, to the rest of the engagement team on a timely basis. When the auditor identifies related parties during the audit that were not previously communicated, the auditor should promptly inform the rest of the engagement team.

36. Timely communication and discussion within the engagement team of the outcome of the risk assessment procedures, including the identities of related parties and significant identified risks, are important as such information affects the planning and performance of further audit

procedures. The auditor promptly communicates the names of related parties newly identified during the audit to the rest of the engagement team to enable them to (a) determine whether this new information affects the results and conclusions drawn from other audit procedures, and (b) perform audit procedures designed to identify transactions with such parties.

### **Responses to the Risks of Material Misstatement Due to Related Parties**

37. ISA 330, “The Auditor’s Procedures in Response to Assessed Risks,” requires the auditor to design and perform audit procedures whose nature, timing, and extent respond to the assessed risks of material misstatement at both the financial statement and assertion levels. This ISA focuses on specific responses at the assertion level only.

#### *Consideration of Materiality in Responding to Assessed Risks*

38. When examining a related party transaction, the auditor considers both the quantitative and qualitative aspects of the materiality of the transaction, as (a) the monetary value of the transaction may not be relevant in evaluating the significance of the transaction, or (b) there may be no objective basis for measuring the transaction. For example, the applicable financial reporting framework may deem transactions between the entity and those charged with governance to be material regardless of the amounts involved.

#### *Testing the Operating Effectiveness of Internal Control*

39. ISA 330 requires the auditor to perform tests of control when:

- (a) The auditor’s assessment of risks of material misstatement at the assertion level is based on an expectation that controls over the process of identifying and disclosing related party relationships and transactions are operating effectively; or
- (b) Substantive procedures alone do not provide sufficient appropriate audit evidence at the assertion level.

40. Testing the operating effectiveness of the entity’s controls over this process is likely to be an appropriate response when, for example:

- Controls exist for the review and approval of related party transactions by appropriate levels of management and, where appropriate, those charged with governance.
- Information necessary for preparing related party disclosures is derived from the routine processing of data by the entity’s information accounting system.

41. When performing tests of the operating effectiveness of controls, the auditor obtains audit evidence sufficient to determine whether the controls operated effectively throughout the reporting period. This includes obtaining audit evidence about (a) how controls were applied at relevant times during the period under audit, (b) the consistency with which they were applied, and (c) by whom they were applied. Guidance on testing controls is set out in paragraphs 28-47 of ISA 330.

*Substantive Procedures Responsive to Assessed Risks*

42. To respond to the ~~assessed risks of material misstatement due to that~~ related parties relationships and transactions may not have been identified and appropriately disclosed, the auditor should:

- (a) ~~Inquire of management, those charged with governance, internal audit, and others within the entity, regarding the existence of undisclosed related party relationships or transactions~~ Review third party confirmations and other relevant documentation for evidence of related party relationships or transactions; and
- (b) ~~Perform other audit procedures designed to identify significant and unusual transactions, and determine whether related parties are involved~~ Review third party confirmations and other relevant documentation for guarantor relationships and other related party relationships or transactions.

43. Third party confirmations and other relevant documentation that the auditor reviews include:

- (a) Bank and legal confirmations;
- (b) Minutes of meetings of shareholders, management and those charged with governance;
- (c) Invoices and correspondence from law firms;
- (d) Income tax returns and other information supplied to regulatory authorities;
- (e) Significant contracts and agreements not in the ordinary course of business, including those involving management and those charged with governance; and
- (f) Other documentation considered appropriate, such as internal audit working papers.

44. ~~Inquiring of management, those charged with governance, internal audit, and others within the entity is appropriate to respond to the risk that related party transactions may have occurred but not been recorded or disclosed to the auditor. Related party~~ Examples of significant and unusual transactions that may not be recorded or disclosed involve related parties include:

- Transactions that appear designed or structured to achieve specific accounting outcomes.
- Transactions from which management stands to receive a significant financial gain.
- Transactions where no consideration is exchanged, for example, the leasing of premises or the rendering of management services by the entity to ~~a component~~ another party at no charge.
- Circular ~~or round-trip~~ transactions, for example, sales where the entity funds the full price payable by the other party to the transaction ~~advancing a short-term loan to a related party during the reporting period that is fully repaid before the period end.~~
- ~~Transactions with related parties in which management has a financial interest.~~

45. The procedures set out in paragraph 43 may assist in identifying significant and unusual transactions. Other procedures that the auditor may perform to identify these transactions include:

- Inquiring of personnel who initiate, process or record these transactions, and those who supervise or monitor such personnel.



- Inquiring of non-financial personnel of the entity regarding their knowledge of significant and unusual transactions.
- Conducting a detailed review of accounting records for transactions with specific characteristics, such as terms that deviate significantly from known market terms. Such a review may be facilitated using computer-assisted audit techniques.

~~44. Third party confirmations and other relevant documentation that the auditor reviews include:~~

- ~~• Bank and legal confirmations;~~
- ~~• Minutes of meetings of shareholders, management and those charged with governance;~~
- ~~• Income tax returns and other information supplied to regulatory authorities;~~
- ~~• Significant contracts and agreements not in the ordinary course of business, including those involving management and those charged with governance; and~~
- ~~• Other documentation considered appropriate, such as internal audit working papers.~~

~~465.~~ The extent of the procedures in paragraph 42 will be more limited if (a) tests of controls have been performed, and (b) appropriate audit evidence of effective operation of controls during the reporting period has been obtained.

### Responses to Significant Risks

~~476.~~ Where the auditor has identified significant risks of material misstatement due to related parties, the auditor:

- (a) To the extent not already done, (i) evaluates the design of the entity's controls over related party relationships and transactions, and (ii) determines whether they have been implemented (paragraph 113 of ISA 315);
- (b) Obtains audit evidence about the operating effectiveness of these controls (on which the auditor plans to rely) from tests of control performed in the current period (paragraph 44 of ISA 330); and
- (c) Performs substantive procedures that specifically respond to the significant risks (paragraph 51 of ISA 330 and paragraphs ~~487-523~~ of this ISA).

### *Substantive Procedures to Respond to Significant Risks*

~~4847.~~ When the auditor ~~For~~ identifies significant and unusual transactions that give rise to significant risks due to related parties, the auditor should:

- ~~(a) Obtain an understanding of the nature and substance of the transactions; and~~
- ~~(b) Consider obtaining corroborative audit evidence regarding the nature and substance of the transactions, by:~~
  - ~~(i) Confirming the purposes, terms, and amounts of the transactions with the other parties;~~
  - ~~(ii) Inspecting evidence in the possession of the other parties;~~
  - ~~(iii) Confirming or discussing information with intermediaries such as banks, law firms, guarantors, or agents;~~



- ~~(iv) — Reviewing the financial statements of the other parties to the transactions; and~~  
~~(v) Inquiring of other information sources, such as industry news sources, credit agencies and persons providing professional advice to the entity.~~

49. This requirement complements the requirement in paragraph 76 of ISA 240 for the auditor to understand the business rationale of the transactions.

50. Procedures that the auditor may perform to obtain corroborative audit evidence include:

- Confirming the purposes, terms, and amounts of the transactions with the other parties.
- Inspecting information in the possession of the other parties.
- Confirming or discussing relevant information with intermediaries such as banks, law firms, guarantors, or agents.
- Reading the financial statements or other relevant financial information of the other parties to the transactions.
- Inquiring of other information sources, such as industry news sources, credit agencies and persons providing professional advice to the entity.

~~48. In understanding the nature and substance of the transactions, the auditor:~~

- ~~(a) Inquires of management and those charged with governance regarding the business purposes of the transactions;~~  
~~(b) Inspects invoices, contracts and agreements, and other relevant documentation of the transactions to understand their financial effects;~~  
~~(c) Determines whether the transactions have been appropriately approved; and~~  
~~(d) Considers other relevant information obtained from performing other audit procedures that may provide evidence regarding the nature and substance of the transactions.~~  
 49. In considering the other parties to the transactions as a source of audit evidence, the auditor takes into account the potential lack of reliability of the evidence if the parties are in fact related, as such parties may be biased or be otherwise influenced by management.

520. In considering the inspection of evidence information in the possession of the other parties, the auditor considers whether appropriate access to the information evidence will be granted by the other parties, and requests management's permission to seek to obtain such access. Where such access is granted, the auditor may consider, for example:

- Inspecting relevant records and making appropriate inquiries of the other parties regarding the transactions that might confirm the identity of the other parties and the nature and substance of the transactions.
- Verifying the existence of the assets or inspecting their condition if the transactions involve asset sales, to obtain corroborative audit evidence regarding the reasonableness of the terms of the transactions.

~~51. When the auditor obtains information from performing other audit procedures that indicates a significant risk that undisclosed related party transactions may exist, the auditor should perform additional audit procedures to respond to that risk.~~

~~52. The nature and extent of the additional audit procedures that the auditor performs will vary with factors such as:~~

- ~~• The nature of the information obtained;~~
- ~~• The evidence obtained from the other audit procedures performed;~~
- ~~• The characteristics of the class of transactions involved; and~~
- ~~• Whether to request management to perform further work to provide additional information from the accounting records, for example, transactions with specific parties.~~

~~53. Examples of additional audit procedures include:~~

- ~~• Conducting a detailed review of accounting records for transactions with specific characteristics, such as terms that deviate from known market terms. Such a review may be facilitated using computer-assisted audit techniques.~~
- ~~• Testing the additional information that the auditor has requested management to provide for evidence of related party relationships.~~
- ~~• Designing external confirmations to confirm the existence of related party arrangements with specific parties.~~
- ~~• Inquiring of non-financial personnel of the entity regarding details of specific transactions.~~

#### **Identification of Previously Undisclosed Related Party Relationships or Transactions**

~~54. Throughout the audit, the auditor should be alert for transactions that appear unusual as they may indicate the existence of previously unidentified related parties.~~

~~535.~~ When the auditor identifies related party relationships or transactions not previously recorded and disclosed by the entity, the auditor should:

- (a) Investigate why the entity's internal control had not identified them; and
- (b) Determine whether it is necessary to reassess the risks of material misstatement due to related parties.

**If these risks are reassessed, the auditor should consider the implications for other aspects of the audit, including the reliance placed on other representations made by management and those charged with governance during the audit.**

~~56. ISA 315 provides guidance when the auditor identifies material weaknesses in the entity's internal control.~~

#### **Measurement Considerations**

54. Related party transactions occurring as part of the normal course of business ordinarily can be readily measured and recorded at the amounts indicated by their terms. For some related party

transactions, however, the value of the consideration exchanged may not be readily determinable for a number of reasons, including the following:

- There is no exchange of consideration.
- The consideration exchanged is non-monetary in nature.
- There is no objective basis of measurement of the fair value of the consideration exchanged.

55. In these circumstances, the auditor considers whether the applicable financial reporting framework provides requirements and guidance for the appropriate measurement of such transactions. Where the framework addresses the measurement of the transactions, the auditor evaluates whether they have been appropriately accounted for and recorded in accordance with that framework. Where the framework does not deal with the measurement of the transactions, the auditor considers whether they have been appropriately disclosed, in accordance with paragraphs 68-76.

#### **Disclosures Asserting Related Party Transactions to be at Arm's Length**

567. When disclosures of related party transactions **assert state or otherwise suggest** that the transactions ~~have been were~~ conducted at arm's length, the auditor should be satisfied that such assertion is substantiated.

578. Management is responsible for substantiating any assertion that a related party transaction was conducted at arm's length. Such assertion may explicitly state that the transaction was at arm's length or otherwise suggest that the transaction was consummated on terms equivalent or similar to those prevailing in transactions with unrelated parties. The auditor tests management's process for making the assertion to obtain sufficient appropriate audit evidence that the assertion is substantiated.

589. Testing the process used to make the arm's length assertion involves the following:

- (a) Considering the appropriateness of management's methodology for substantiating the arm's length basis;
- (b) Verifying the source of the internal or external data supporting the assertion, and testing the data to determine their accuracy, completeness and relevance; and
- (c) When the substantiation rests on significant assumptions, considering whether they reasonably support the assertion.

5960. Management may substantiate the arm's length assertion in various ways, such as:

- Comparing the terms of the related party transaction to those of an identical transaction with one or more ~~independent-unrelated~~ parties;
- Engaging an external expert to determine a market value for the transaction; or
- Comparing the terms of the transaction to known market terms for broadly similar transactions on an open market.

~~604.~~ The form and nature of a related party transaction often make it impracticable for management to objectively substantiate ~~an-the~~ arm's length assertion.

~~612.~~ When the auditor is unable to obtain sufficient appropriate audit evidence to substantiate management's assertion that a related party transaction has been conducted at arm's length, the auditor should request that management ~~to~~ withdraw the assertion. If management disagrees, the auditor should consider the implications for the auditor's report (see Proposed ISA 7051, "Modifications to the Opinion in the Independent Auditor's Report").

#### Communications with Those Charged with Governance

~~623.~~ The auditor should discuss with those charged with governance the nature, extent and substance of significant related party transactions, including those involving actual or perceived conflicts of interest ~~with those charged with governance related party transactions that:~~

- ~~(a) Are not in the ordinary course of business; or~~
- ~~(b) Involve actual or perceived conflicts of interest.~~

~~634.~~ ~~The~~ ~~Such a~~ discussion ~~addresses the nature, substance and disclosure of these transactions. It~~ enables the auditor to:

- ~~(a)~~ Confirm that those charged with governance are fully aware of the extent to which related party transactions have affected the financial statements, or alternatively bring such information to their attention;
- ~~(ba)~~ Establish a common understanding with those charged with governance of the propriety of the transactions, especially those involving actual or perceived conflicts of interest, and their risks and ~~potential~~ effects on the financial statements;
- ~~(cb)~~ Alert those charged with governance to specific related party relationships and transactions of which they may not have been aware, to enable them to take appropriate action where necessary;
- ~~(de)~~ Comment on the completeness, accuracy and adequacy of management's related party disclosures;
- ~~(ed)~~ Resolve identified related party issues, such as disagreements regarding the nature and extent of disclosure, on a timely basis; and
- ~~(fe)~~ Where applicable, corroborate responses from management to inquiries the auditor has made into such-related party matters.

~~65.~~ ~~ISA 260, "Communication of Audit Matters with Those Charged with Governance," provides guidance on the auditor's responsibilities regarding communications with those charged with governance.~~

## Written Representations

~~64~~6. The auditor should obtain ~~a~~-written representations from management and, where appropriate, those charged with governance ~~regarding~~concerning:

- (a) The completeness of information provided to the auditor regarding identified related parties and transactions with such parties; and
- (b) ~~¶~~The completeness, accuracy and adequacy of related party disclosures in the financial statements.

65. The auditor may also consider obtaining written representations concerning relevant related party matters from one or more of the entity's shareholders, when they do not form part of management or those charged with governance.

~~66~~7. Written representations include confirmation from management and, where appropriate, those charged with governance that they have disclosed to the auditor all relevant information relating to identified related parties ~~iesy relationships and transactions~~, and that they are not aware of any other related party matters required to be disclosed in the financial statements in accordance with the applicable financial reporting framework. Such representations emphasize to management and, where appropriate, those charged with governance their responsibility to disclose the identities of related parties to the auditor even if there have been no transactions with such parties. The representations may ~~also~~ address, where appropriate, specific related party issues, such as the existence of undisclosed side agreements on significant ~~identified~~ related party transactions.

67. Circumstances in which it may be appropriate to obtain written representations from those charged with governance and shareholders include:

- When they have approved specific related party transactions that (a) materially affect the financial statements, or (b) involve management.
- When they have made specific oral representations to the auditor regarding details of certain related party transactions.
- When they have financial or other interests in the related party transactions.

## Evaluation of Related Party Disclosures and Reporting

*~~Render~~Expressing an Opinion on the Fair Presentation of the Financial Statements Prepared in Accordance with a Financial Reporting Framework Designed to Achieve Fair Presentation*

68. When the objective of the engagement is to report on ~~express an audit opinion on whether the financial statements give a true and fair view, or are presented fairly, in all material respects, prepared~~ in accordance with the applicable financial reporting framework designed to achieve fair presentation, the auditor should evaluate whether the related party disclosures in the financial statements ~~are fairly presented~~ are presented in a manner that achieves fair presentation of the financial statements.

69. As the underlying financial reporting framework is designed to achieve fair presentation, it is necessary for the auditor to evaluate whether the related party disclosures appropriately support this objective~~As discussed in ISA 700, “The Independent Auditor’s Report on a Complete Set of General Purpose Financial Statements,” determining whether the financial statements give a true and fair view or are presented fairly, in all material respects, in accordance with the applicable financial reporting framework involves evaluating the fair presentation of the financial statements.~~ In making this evaluation, the auditor considers whether the entity’s related party disclosures~~of the entity’s related party transactions are:~~
- (a) Reflect the substance of the related party transactions, particularly if substance differs from form;
  - (~~a~~b) Are~~C~~ complete and accurate in accordance with the requirements of the applicable financial reporting framework; and
  - (~~b~~) ~~Consistent with the auditor’s understanding of the facts and substance of the transactions; and~~
  - (c) Reasonably summarize the facts and circumstances of the related party transactions so that they are Understandable and not misleading.
70. Disclosures of R~~related party transactions disclosures~~ may be potentially misleading if (a) the substance and the effects of the ~~related party~~ transactions on the financial statements are unclear or misstated, or (b) key terms, conditions, or other important elements of the transactions necessary for understanding them are not appropriately disclosed. Accordingly, in drawing a conclusion regarding whether the fair presentation of the related party disclosures appropriately support the fair presentation of the financial statements, the auditor evaluates whether the disclosures faithfully represent the related party relationships and transactions in a manner that gives a true and fair view of, or presents fairly, in all material respects, the information conveyed in the financial statements.
71. If the auditor concludes that achieving the objective of fair presentation of the financial statements requires (a) changes to the related party disclosures, or (b) additional disclosures not required by the applicable financial reporting framework, the auditor discusses these changes and additional disclosures with management.
72. **If management refuses to make the changes or additional disclosures necessary to achieve fair presentation of the financial statements, the auditor should consider the implications for the auditor’s report (see Proposed ISA 70~~51~~).**
- ~~Render~~Expressing an Opinion ~~Whether the on~~ Financial Statements ~~Comply with the Applicable Prepared in Accordance with a~~ Financial Reporting Framework not Designed to Achieve Fair Presentation
73. **When the only objective of the engagement is to express an audit opinion whether the financial statements are prepared, in all material respects, in accordance with ~~the applicable a~~ financial reporting framework not designed to achieve fair presentation, the auditor should evaluate whether the related party disclosures in the financial statements are complete and accurate, and comply with the requirements of that framework.**

74. Where the auditor is only required to report whether the financial statements are prepared, in all material respects, in accordance with ~~the applicable a~~ financial reporting framework not designed to achieve fair presentation, the auditor has no responsibility to evaluate whether the entity's related party disclosures are presented in a manner that achieves fair presentation of the financial statements. The auditor considers, however, whether the related party disclosures are complete and accurate in respect of the specific elements of the related party relationships and transactions required to be disclosed by the financial reporting framework.
75. If the auditor concludes that the entity's related party disclosures do not comply with the requirements of the applicable financial reporting framework, the auditor discusses with management the changes necessary to achieve compliance.
76. **If management refuses to make the changes in the related party disclosures necessary for compliance with the requirements of the applicable financial reporting framework, the auditor should consider the implications for the auditor's report (see Proposed ISA 705~~51~~).**

*Inability to Obtain Sufficient Appropriate Audit Evidence Regarding Related Party Disclosures*

77. Because of the nature and characteristics of related party relationships and transactions, the auditor considers whether circumstances arose during the audit that resulted in an inability to obtain sufficient appropriate audit evidence to address the risks of material misstatement due to related parties. Such a limitation in the scope of the audit may arise, for example, when the auditor has assessed a significant risk of material misstatement due to related parties and determines that testing relevant controls is a necessary audit procedure, but is unable to do so, as (a) the internal control system has not been designed to identify, record, summarize and disclose related party relationships and transactions, or (b) the design or implementation of the internal control system is inadequate for that purpose. A scope limitation may also be imposed by management in respect of related party transactions that management considers sensitive, for example, when the transactions involve management in a conflict of interest or fraud. Proposed ISA 705 provides guidance on modifications to the opinion in the independent auditor's report when there is a scope limitation.

**Effective Date**

- ~~78~~7. This ISA is effective for audits of financial statements for periods commencing on or after [ ]. Early application of this ISA is permitted.

## Appendix 1

### Definitions Adopted from IAS 24 (Revised)

Related party – A party is related to an entity if:

- a) directly, or indirectly through one or more intermediaries, the party:
  - i) controls, is controlled by, or is under common control with, the entity (this includes parents, subsidiaries and fellow subsidiaries);
  - ii) has an interest in the entity that gives it significant influence over the entity; or
  - iii) has joint control over the entity;
- b) the party is an associate (as defined in IAS 28, “Investments in Associates”) of the entity;
- c) the party is a joint venture in which the entity is a venturer (see IAS 31, “Interests in Joint Ventures”);
- d) the party is a member of the key management personnel of the entity or its parent;
- e) the party is a close member of the family of any individual referred to in (a) or (d);
- f) the party is an entity that is controlled, jointly controlled or significantly influenced by, or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or
- g) the party is a post-employment benefit plan for the benefit of employees of the entity, or of any entity that is a related party of the entity.

A related party transaction is a transfer of resources, services or obligations between related parties, regardless of whether a price is charged.

Close members of the family of an individual are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity. They may include:

- a) the individual's domestic partner and children;
- b) children of the individual's domestic partner; and
- c) dependants of the individual or the individual's domestic partner.

Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Joint control is the contractually agreed sharing of control over an economic activity.

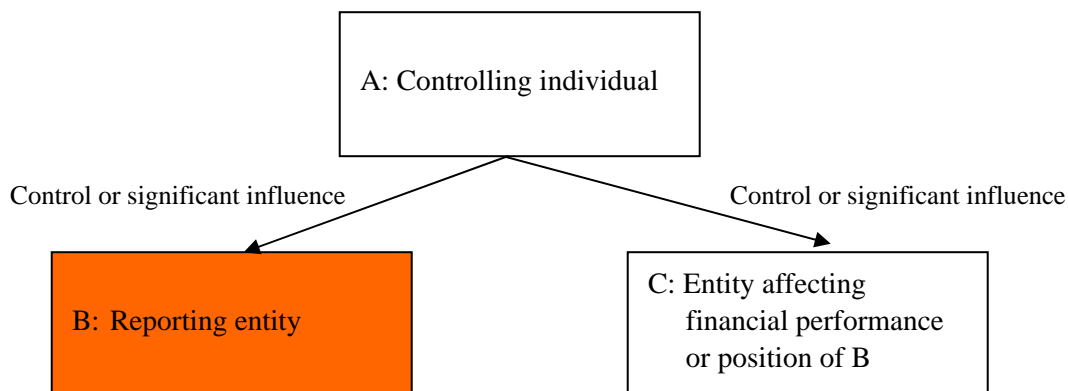
Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity.



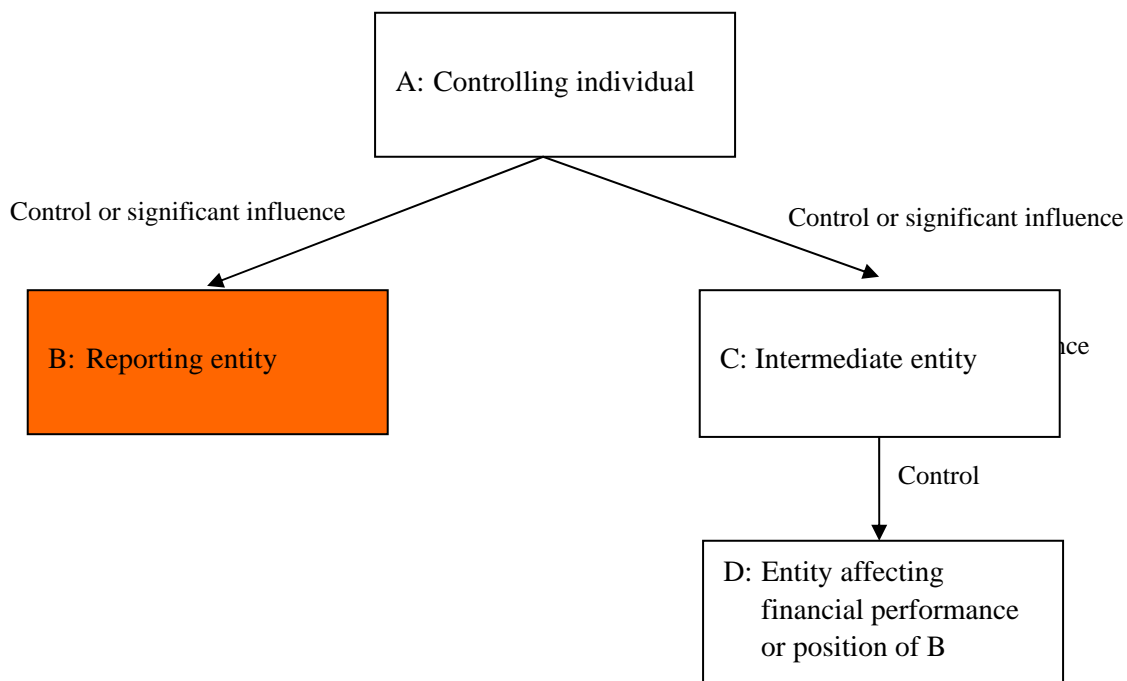
Significant influence is the power to participate in the financial and operating policy decisions of an entity, but is not control over those policies. Significant influence may be gained by share ownership, statute or agreement.

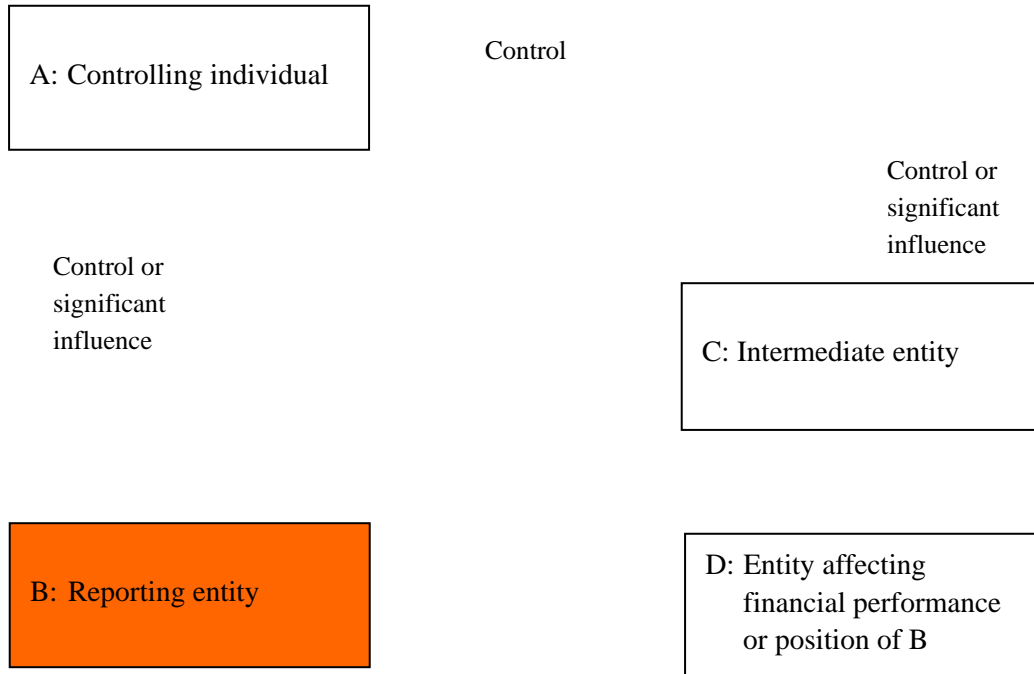
## Appendix 2

### Examples of Horizontal Groups

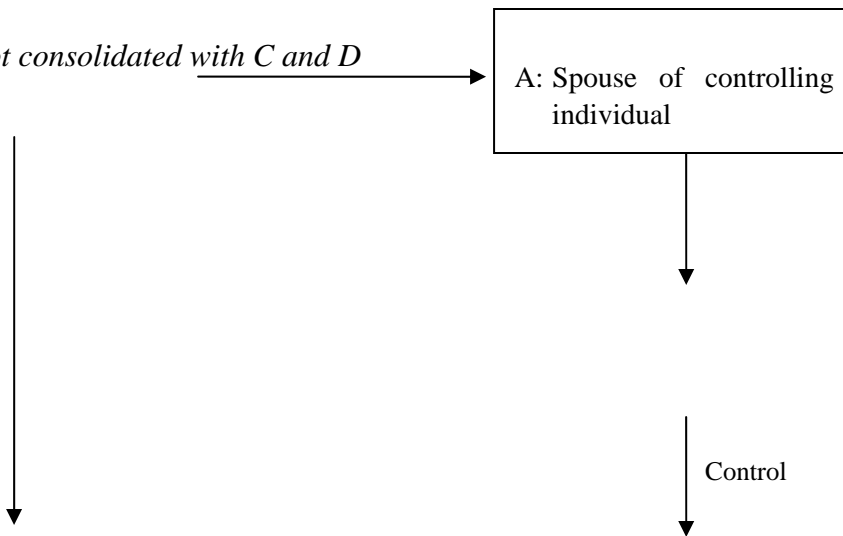


*Illustration 1: B and C are not consolidated*





*Illustration 2: B is not consolidated with C and D*



## Appendix 3

### Examples of Related Party Risk Factors

In addition to the risk factors listed in paragraph ~~2830~~, the following is a non-exhaustive list of other factors the auditor may consider in identifying the risks of material misstatement of the financial statements due to related parties. Not all of these examples are relevant in all circumstances, and some may be of greater or lesser significance in entities of different sizes, with different ownership characteristics, in different industries, or because of other differing characteristics or circumstances. Risk factors that are specific to the entity and not listed below should also be considered. In addition, certain risk factors listed in Appendix 1 of ISA 240 that are not listed below may also be relevant.

- Generally, circular arrangements such as:
  - ~~Sales that include funding of the full price payable by the other party to the transaction.~~
  - Sales with a commitment to repurchase that, if known, would preclude recognition of all or part of the revenue.
  - Advancing funds that are subsequently transferred to a debtor and used to repay what would otherwise be an uncollectible loan or receivable.
  - Obtaining loans immediately before the period end that are fully repaid shortly after.
- Generally, conditions that indicate transactions are not at arm's length, such as:
  - Borrowing or lending money interest-free or at a rate of interest significantly above or below prevailing market rates.
  - Selling real estate at a price that differs significantly from its appraised value.
  - Purchases, sales or other transactions at prices in excess of or below fair market value.
- Generally, the absence of substance, such as:
  - Loans made with no scheduled repayment terms.
  - Loans advanced to parties having no ability to repay, or transactions that have remained unsettled for a considerable period of time.
  - Loans apparently advanced for a valid business purpose and later written off as uncollectible.
  - Payments for services never rendered.
- Indications of other unusual terms, conditions or circumstances, such as:
  - Absence of competitive bidding on significant contracts.
  - Exchange of property for similar property in a non-monetary transaction.
  - Sales to an unnecessary “middle man” related party, who in turn sells to the ultimate customer at a higher price, where the related party retains the difference.
  - Agreements under which one party pays another party's expenses.
  - Unusual arrangements with certain parties to mitigate market risks.

- Unusual transactions at or close to the period end.
- Indications of changes in the terms of the transactions, particularly if they no longer reflect normal commercial terms.
- The lack of relevant documentation.
- An unwarranted emphasis on secrecy or confidentiality.

**[Blank Page]**