

**INTERNATIONAL STANDARD ON AUDITING 600 (REVISED),  
SPECIAL CONSIDERATIONS—AUDITS OF GROUP FINANCIAL  
STATEMENTS (INCLUDING THE WORK OF COMPONENT  
AUDITORS)**

**[Approved by IAASB]**

## Introduction

### Scope of this ISA

1. The International Standards on Auditing (ISAs) apply to an audit of group financial statements (a group audit). This ISA deals with special considerations that apply to a group audit, including in those circumstances when component auditors are involved. The requirements and guidance in this ISA refer to, or expand on, the application of other relevant ISAs to a group audit, in particular ISA 220 (Revised),<sup>1</sup> ISA 230,<sup>2</sup> ISA 300,<sup>3</sup> ISA 315 (Revised 2019),<sup>4</sup> and ISA 330.<sup>5</sup> (Ref: Para. A1–A2)
2. Group financial statements include the financial information of more than one entity or business unit through a consolidation process, as described in paragraph 14(k). The term consolidation process as used in this ISA refers not only to the preparation of consolidated financial statements in accordance with the applicable financial reporting framework, but also to the presentation of combined financial statements, and to the aggregation of the financial information of entities or business units such as branches or divisions. (Ref: Para. A3–A5, A25)
3. As explained in ISA 220 (Revised),<sup>6</sup> this ISA, adapted as necessary in the circumstances, may also be useful in an audit of financial statements other than a group audit when the engagement team includes individuals from another firm. For example, this ISA may be useful when involving such an individual to attend a physical inventory count, inspect property, plant and equipment, or perform audit procedures at a shared service center at a remote location.

### *Groups and Components*

4. A group may be organized in various ways. For example, a group may be organized by legal or other entities (e.g., a parent and one or more subsidiaries, joint ventures, or investments accounted for by the equity method). Alternatively, the group may be organized by geography, by other economic units (including branches or divisions), or by functions or business activities. In this ISA, these different forms of organization are collectively referred to as “entities or business units.” (Ref: Para. A6)
5. The group auditor determines an appropriate approach to planning and performing audit procedures to respond to the assessed risks of material misstatement of the group financial statements. For this purpose, the group auditor uses professional judgment in determining the components at which audit work will be performed. This determination is based on the group auditor’s understanding of the group and its environment, and other factors such as the ability to

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<sup>1</sup> ISA 220 (Revised), *Quality Management for an Audit of Financial Statements*

<sup>2</sup> ISA 230, *Audit Documentation*

<sup>3</sup> ISA 300, *Planning an Audit of Financial Statements*

<sup>4</sup> ISA 315 (Revised 2019), *Identifying and Assessing the Risks of Material Misstatement*

<sup>5</sup> ISA 330, *The Auditor’s Responses to Assessed Risks*

<sup>6</sup> ISA 220 (Revised), paragraph A1

perform audit procedures centrally, the presence of shared service centers, or the existence of common information systems and internal control. (Ref: Para. A7–A9)

#### *Involvement of Component Auditors*

6. ISA 220 (Revised)<sup>7</sup> requires the engagement partner to determine that sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team in a timely manner. In a group audit, such resources may include component auditors. Therefore, this ISA requires the group auditor to determine the nature, timing and extent of involvement of component auditors.
7. The group auditor may involve component auditors to provide information, or to perform audit work, to fulfill the requirements of this ISA. Component auditors may have greater experience with, and a more in-depth knowledge of, the components and their environments (including local laws and regulations, business practices, language, and culture) than the group auditor. Accordingly, component auditors can be, and often are, involved in all phases of the group audit. (Ref: Para. A10–A10A)
8. Audit risk is a function of the risks of material misstatement and detection risk.<sup>8</sup> Detection risk in a group audit includes the risk that a component auditor may not detect a misstatement in the financial information of a component that could cause a material misstatement of the group financial statements, and that the group auditor may not detect this misstatement. Accordingly, this ISA requires sufficient and appropriate involvement by the group engagement partner or group auditor, as applicable, in the work of component auditors and emphasizes the importance of two-way communication between the group auditor and component auditors. In addition, this ISA explains the matters that the group auditor takes into account when determining the nature, timing and extent of the direction and supervision of component auditors and the review of their work. (Ref: Para. A11–A12)

#### *Professional Skepticism*

9. In accordance with ISA 200,<sup>9</sup> the engagement team is required to plan and perform the group audit with professional skepticism and to exercise professional judgment. The appropriate exercise of professional skepticism may be demonstrated through the actions and communications of the engagement team, including emphasizing the importance of each engagement team member exercising professional skepticism throughout the group audit. Such actions and communications may include specific steps to mitigate impediments that may impair the appropriate exercise of professional skepticism. (Ref: Para. A13–A17)

#### *Scalability*

10. This ISA is intended for all group audits, regardless of size or complexity. However, the requirements of this ISA are intended to be applied in the context of the nature and circumstances of each group audit. For example, when a group audit is carried out entirely by the group auditor, some requirements in this ISA are not relevant because they are conditional on the involvement of component auditors. This may be the case when the group auditor is able to perform audit procedures centrally or is able to perform procedures at the components without involving

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<sup>7</sup> ISA 220 (Revised), paragraph 25

<sup>8</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraph A34

<sup>9</sup> ISA 200, paragraphs 15–16

component auditors. The guidance in paragraphs A117 and A118 also may be helpful in applying this ISA in these circumstances.

#### *Responsibilities of the Group Engagement Partner and Group Auditor*

11. The group engagement partner remains ultimately responsible, and therefore accountable, for compliance with the requirements of this ISA. The term “the group engagement partner shall take responsibility for...” or “the group auditor shall take responsibility for...” is used for those requirements when the group engagement partner or group auditor, respectively, is permitted to assign the design or performance of procedures, tasks or actions to other appropriately skilled or suitably experienced members of the engagement team, including component auditors. For other requirements, this ISA expressly intends that the requirement or responsibility be fulfilled by the group engagement partner or group auditor, as applicable, and the group engagement partner or group auditor may obtain information from the firm or other members of the engagement team. (Ref: Para. A27)

#### **Effective Date**

12. This ISA is effective for audits of group financial statements for periods beginning on or after December 15, 2023.

#### **Objectives**

13. The objectives of the auditor are to:
  - (a) With respect to the acceptance and continuance of the group audit engagement, determine whether sufficient appropriate audit evidence can reasonably be expected to be obtained to provide a basis for forming an opinion on the group financial statements;
  - (b) Identify and assess the risks of material misstatement of the group financial statements, whether due to fraud or error, and plan and perform further audit procedures to appropriately respond to those assessed risks;
  - (c) Be sufficiently and appropriately involved in the work of component auditors throughout the group audit, including communicating clearly about the scope and timing of their work, and evaluating the results of that work; and
  - (d) Evaluate whether sufficient appropriate audit evidence has been obtained from the audit procedures performed, including with respect to the work performed by component auditors, as a basis for forming an opinion on the group financial statements.

#### **Definitions**

14. For purposes of the ISAs, the following terms have the meanings attributed below:
  - (a) Aggregation risk – The probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. (Ref: Para. A18)
  - (b) Component – An entity, business unit, function or business activity, or some combination thereof, determined by the group auditor for purposes of planning and performing audit procedures in a group audit. (Ref: Para. A19)

- (c) Component auditor – An auditor who performs audit work related to a component for purposes of the group audit. A component auditor is a part of the engagement team<sup>10</sup> for a group audit. (Ref: Para. A20–A21A)
  - (d) Component management – Management responsible for a component. (Ref: Para. A22)
  - (e) Component performance materiality – An amount set by the group auditor to reduce aggregation risk to an appropriately low level for purposes of planning and performing audit procedures in relation to a component.
  - (f) Group – A reporting entity for which group financial statements are prepared.
  - (g) Group audit – The audit of group financial statements.
  - (h) Group auditor – The group engagement partner and members of the engagement team other than component auditors. The group auditor is responsible for:
    - (i) Establishing the overall group audit strategy and group audit plan;
    - (ii) Directing and supervising component auditors and reviewing their work;
    - (iii) Evaluating the conclusions drawn from the audit evidence obtained as the basis for forming an opinion on the group financial statements.
  - (i) Group audit opinion – The audit opinion on the group financial statements.
  - (j) Group engagement partner – The engagement partner<sup>11</sup> who is responsible for the group audit. (Ref: Para. A23)
  - (k) Group financial statements – Financial statements that include the financial information of more than one entity or business unit through a consolidation process. For purposes of this ISA, a consolidation process includes: (Ref: Para. A24–A26)
    - (i) Consolidation, proportionate consolidation, or an equity method of accounting;
    - (ii) The presentation in combined financial statements of the financial information of entities or business units that have no parent but are under common control or common management; or
    - (iii) The aggregation of the financial information of entities or business units such as branches or divisions.
  - (l) Group management – Management responsible for the preparation of the group financial statements.
  - (m) Group performance materiality – Performance materiality<sup>12</sup> in relation to the group financial statements as a whole, as determined by the group auditor.
15. Reference in this ISA to “the applicable financial reporting framework” means the financial reporting framework that applies to the group financial statements.

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<sup>10</sup> ISA 220 (Revised), paragraph 12(d)

<sup>11</sup> ISA 220 (Revised), paragraph 12(a)

<sup>12</sup> ISA 320, *Materiality in Planning and Performing an Audit*, paragraphs 9 and 11

## Requirements

### Leadership Responsibilities for Managing and Achieving Quality on a Group Audit

16. In applying ISA 220 (Revised),<sup>13</sup> the group engagement partner is required to take overall responsibility for managing and achieving quality on the group audit engagement. In doing so, the group engagement partner shall: (Ref: Para. A27–A28)
- (a) Take responsibility for creating an environment for the group audit engagement that emphasizes the expected behavior of engagement team members. (Ref: Para. A29)
  - (b) Be sufficiently and appropriately involved throughout the group audit engagement, including in the work of component auditors, such that the group engagement partner has the basis for determining whether the significant judgments made, and the conclusions reached, are appropriate given the nature and circumstances of the group audit engagement.

### Acceptance and Continuance

17. Before accepting or continuing the group audit engagement, the group engagement partner shall determine whether sufficient appropriate audit evidence can reasonably be expected to be obtained to provide a basis for forming an opinion on the group financial statements. (Ref: Para. A30–A33)
18. If, after the acceptance or continuance of the group audit engagement, the group engagement partner concludes that sufficient appropriate audit evidence cannot be obtained, the group engagement partner shall consider the possible effects on the group audit. (Ref: Para. A34)

### Terms of the Engagement

19. In applying ISA 210,<sup>14</sup> the group auditor shall obtain the agreement of group management that it acknowledges and understands its responsibility to provide the engagement team with: (Ref: Para. A35)
- (a) Access to all information of which group management is aware that is relevant to the preparation of the group financial statements such as records, documentation and other matters;
  - (b) Additional information that the engagement team may request from group management or component management for the purpose of the group audit; and
  - (c) Unrestricted access to persons within the group from whom the engagement team determines it necessary to obtain audit evidence.

### Restrictions on Access to Information or People Outside the Control of Group Management

20. If the group engagement partner concludes that group management cannot provide the engagement team with access to information or unrestricted access to persons within the group due to restrictions that are outside the control of group management, the group engagement partner shall consider the possible effects on the group audit. (Ref: Para. A36–A43)

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<sup>13</sup> ISA 220 (Revised), paragraph 13

<sup>14</sup> ISA 210, *Agreeing the Terms of Audit Engagements*, paragraphs 6(b) and 8(b)

*Restrictions on Access to Information or People Imposed by Group Management*

21. If the group engagement partner concludes that: (Ref: Para. A41–A43)
- (a) It will not be possible for the group auditor to obtain sufficient appropriate audit evidence due to restrictions imposed by group management; and
  - (b) The possible effect of this limitation will result in a disclaimer of opinion on the group financial statements,
- the group engagement partner shall either:
- (i) In the case of an initial engagement, not accept the engagement, or, in the case of a recurring engagement, withdraw from the engagement, when withdrawal is possible under applicable law or regulation; or
  - (ii) When law or regulation prohibit an auditor from declining an engagement or when withdrawal from an engagement is not otherwise possible, having performed the audit of the group financial statements to the extent possible, disclaim an opinion on the group financial statements.

**Overall Group Audit Strategy and Group Audit Plan**

22. In applying ISA 300,<sup>15</sup> the group auditor shall establish, and update as necessary, an overall group audit strategy and group audit plan. In doing so, the group auditor shall determine: (Ref: Para. A44–A47)
- (a) The components at which audit work will be performed; and (Ref: Para. A48)
  - (b) The resources needed to perform the group audit engagement, including the nature, timing and extent to which component auditors are to be involved. (Ref: Para. A49–A53)

*Considerations When Component Auditors Are Involved*

23. In establishing the overall group audit strategy and group audit plan, the group engagement partner shall evaluate whether the group auditor will be able to be sufficiently and appropriately involved in the work of the component auditor. (Ref: Para. A54)
24. As part of the evaluation in paragraph 23, the group auditor shall request the component auditor to confirm that the component auditor will cooperate with the group auditor, including whether the component auditor will perform the work requested by the group auditor. (Ref: Para. A55)

**Relevant Ethical Requirements, Including Those Related to Independence**

25. In applying ISA 220 (Revised),<sup>16</sup> the group engagement partner shall take responsibility for: (Ref: Para. A56–A57, A84)
- (a) Component auditors having been made aware of relevant ethical requirements that are applicable given the nature and circumstances of the group audit engagement; and
  - (b) Confirming whether the component auditors understand and will comply with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement.

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<sup>15</sup> ISA 300, paragraphs 7–10A

<sup>16</sup> ISA 220 (Revised), paragraph 17

### Engagement Resources

26. In applying ISA 220 (Revised),<sup>17</sup> the group engagement partner shall: (Ref: Para. A58–A65)
- (a) Determine that component auditors have the appropriate competence and capabilities, including sufficient time, to perform the assigned audit procedures at the component; and
  - (b) If information about the results of the monitoring and remediation process or external inspections related to the component auditor has been provided by the group auditor's firm or has otherwise been made available to the group engagement partner, determine the relevance of such information to the group auditor's determination in paragraph 26(a).
27. The group auditor shall obtain sufficient appropriate audit evidence relating to the work to be performed at the component without involving the component auditor if:
- (a) The component auditor does not comply with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement;<sup>18</sup> or (Ref: Para. A66–A67)
  - (b) The group engagement partner has serious concerns about the matters in paragraphs 23–26. (Ref: Para. A68)

### Engagement Performance

28. In applying ISA 220 (Revised),<sup>19</sup> the group engagement partner shall take responsibility for the nature, timing and extent of direction and supervision of component auditors and the review of their work, taking into account: (Ref: Para. A69–A74)
- (a) Areas of higher assessed risks of material misstatement of the group financial statements, or significant risks identified in accordance with ISA 315 (Revised 2019); and
  - (b) Areas in the audit of the group financial statements that involve significant judgment.

### Communications with Component Auditors

29. The group auditor shall communicate with component auditors about their respective responsibilities and the group auditor's expectations, including an expectation that communications between the group auditor and component auditors take place at appropriate times throughout the group audit. (Ref: Para. A75–A84)

### **Understanding the Group and Its Environment, the Applicable Financial Reporting Framework and the Group's System of Internal Control**

30. In applying ISA 315 (Revised 2019),<sup>20</sup> the group auditor shall take responsibility for obtaining an understanding of the following: (Ref: Para. A85–A89)
- (a) The group and its environment, including: (Ref: Para. A90–A92)
    - (i) The group's organizational structure and its business model, including:
      - a. The locations in which the group has its operations or activities;

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<sup>17</sup> ISA 220 (Revised), paragraphs 25–26

<sup>18</sup> ISA 200, paragraph 14

<sup>19</sup> ISA 220 (Revised), paragraph 29

<sup>20</sup> ISA 315 (Revised 2019), paragraphs 19–27

- b. The nature of the group's operations or activities and the extent to which they are similar across the group; and
- c. The extent to which the group's business model integrates the use of IT;
- (ii) Regulatory factors impacting the entities and business units in the group; and
- (iii) The measures used internally and externally to assess the entities or business units' financial performance;
- (b) The applicable financial reporting framework and the consistency of accounting policies and practices across the group; and
- (c) The group's system of internal control, including:
  - (i) The nature and extent of commonality of controls; (Ref: Para. A93–A97, A100)
  - (ii) Whether, and if so, how, the group centralizes activities relevant to financial reporting; (Ref: Para. A98–A100)
  - (iii) The consolidation process used by the group, including sub-consolidations, if any, and consolidation adjustments; and
  - (iv) How group management communicates significant matters that support the preparation of the group financial statements and related financial reporting responsibilities in the information system and other components of the group's system of internal control to management of entities or business units. (Ref: Para. A101–A103)

*Considerations When Component Auditors Are Involved*

- 31. The group auditor shall communicate to component auditors on a timely basis: (Ref: Para. A104)
  - (a) Matters that the group auditor determines to be relevant to the component auditor's design or performance of risk assessment procedures for purposes of the group audit;
  - (b) In applying ISA 550,<sup>21</sup> related party relationships or transactions identified by group management, and any other related parties of which the group auditor is aware, that are relevant to the work of the component auditor; and (Ref: Para. A105)
  - (c) In applying ISA 570 (Revised),<sup>22</sup> events or conditions identified by group management or the group auditor, that may cast significant doubt on the group's ability to continue as a going concern that are relevant to the work of the component auditor.
- 32. The group auditor shall request component auditors to communicate on a timely basis:
  - (a) Matters related to the financial information of the component that the component auditor determines to be relevant to the identification and assessment of the risks of material misstatement of the group financial statements, whether due to fraud or error;
  - (b) Related party relationships not previously identified by group management or the group auditor; and (Ref: Para. A105)
  - (c) Any events or conditions identified by the component auditor that may cast significant doubt on the group's ability to continue as a going concern.

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<sup>21</sup> ISA 550, *Related Parties*, paragraph 17

<sup>22</sup> ISA 570 (Revised), *Going Concern*

### **Identifying and Assessing the Risks of Material Misstatement**

33. In applying ISA 315 (Revised 2019),<sup>23</sup> based on the understanding obtained in paragraph 30, the group auditor shall take responsibility for the identification and assessment of the risks of material misstatement of the group financial statements, including with respect to the consolidation process. (Ref: Para. A106–A111)

#### *Considerations When Component Auditors Are Involved*

34. In applying ISA 315 (Revised 2019),<sup>24</sup> the group auditor shall evaluate whether the audit evidence obtained from the risk assessment procedures performed by the group auditor and component auditors provides an appropriate basis for the identification and assessment of the risks of material misstatement of the group financial statements. (Ref: Para. A112–A113)

### **Materiality**

35. In applying ISA 320<sup>25</sup> and ISA 450,<sup>26</sup> when classes of transactions, account balances or disclosures in the group financial statements are disaggregated across components, for purposes of planning and performing audit procedures, the group auditor shall determine:
- (a) Component performance materiality. To address aggregation risk, such amount shall be lower than group performance materiality. (Ref: Para. A114–A118)
  - (b) The threshold above which misstatements identified in the component financial information are to be communicated to the group auditor. Such threshold shall not exceed the amount regarded as clearly trivial to the group financial statements. (Ref: Para. A119)

#### *Considerations When Component Auditors Are Involved*

36. The group auditor shall communicate to the component auditor the amounts determined in accordance with paragraph 35. (Ref: Para: A120–A121)

### **Responding to the Assessed Risks of Material Misstatement**

37. In applying ISA 330,<sup>27</sup> the group auditor shall take responsibility for the nature, timing and extent of further audit procedures to be performed, including determining the components at which to perform further audit procedures and the nature, timing and extent of the work to be performed at those components. (Ref: Para. A122–A137)

#### *Consolidation Process*

38. The group auditor shall take responsibility for designing and performing further audit procedures to respond to the assessed risks of material misstatement of the group financial statements arising from the consolidation process. This shall include: (Ref: Para. A138)
- (a) Evaluating whether all entities and business units have been included in the group financial statements as required by the applicable financial reporting framework and, if applicable, for designing and performing further audit procedures on sub-consolidations;

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<sup>23</sup> ISA 315 (Revised 2019), paragraphs 28–34

<sup>24</sup> ISA 315 (Revised 2019), paragraph 35

<sup>25</sup> ISA 320, paragraph 11

<sup>26</sup> ISA 450, *Evaluation of Misstatements Identified during the Audit*, paragraph 5

<sup>27</sup> ISA 330, paragraphs 6–7

- (b) Evaluating the appropriateness, completeness and accuracy of consolidation adjustments and reclassifications; (Ref: Para. A139)
  - (c) Evaluating whether management’s judgments made in the consolidation process give rise to indicators of possible management bias; and
  - (d) Responding to assessed risks of material misstatement due to fraud arising from the consolidation process.
39. If the financial information of an entity or business unit has not been prepared in accordance with the same accounting policies applied to the group financial statements, the group auditor shall evaluate whether the financial information has been appropriately adjusted for purposes of preparing and presenting the group financial statements.
40. If the group financial statements include the financial information of an entity or business unit with a financial reporting period-end that differs from that of the group, the group auditor shall take responsibility for evaluating whether appropriate adjustments have been made to that financial information in accordance with the applicable financial reporting framework.

*Considerations When Component Auditors Are Involved*

41. When the group auditor involves component auditors in the design or performance of further audit procedures, the group auditor shall communicate with the component auditor about matters that the group auditor or component auditor determine to be relevant to the design of responses to the assessed risks of material misstatement of the group financial statements.
42. For areas of higher assessed risks of material misstatement of the group financial statements, or significant risks identified in accordance with ISA 315 (Revised 2019), on which a component auditor is determining the further audit procedures to be performed, the group auditor shall evaluate the appropriateness of the design and performance of those further audit procedures. (Ref: Para. A140)
43. When component auditors perform further audit procedures on the consolidation process, including on sub-consolidations, the group auditor shall determine the nature and extent of direction and supervision of component auditors and the review of their work. (Ref: Para. A141)
44. The group auditor shall determine whether the financial information identified in the component auditor’s communication (see paragraph 45(a)) is the financial information that is incorporated in the group financial statements.

**Evaluating the Component Auditor’s Communications and the Adequacy of Their Work**

45. The group auditor shall request the component auditor to communicate matters relevant to the group auditor’s conclusion with regard to the group audit. Such communication shall include: (Ref: Para. A142)
- (a) Identification of the financial information on which the component auditor has been requested to perform audit procedures;
  - (b) Whether the component auditor has performed the work requested by the group auditor;
  - (c) Whether the component auditor has complied with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement;
  - (d) Information about instances of non-compliance with laws or regulations;
  - (e) Corrected and uncorrected misstatements of the component financial information identified

by the component auditor and that are above the threshold communicated by the group auditor in accordance with paragraph 36; (Ref: Para. A143)

- (f) Indicators of possible management bias;
  - (g) Description of any deficiencies in the system of internal control identified in connection with the audit procedures performed;
  - (h) Fraud or suspected fraud involving component management, employees who have significant roles in the group's system of internal control at the component or others where the fraud resulted in a material misstatement of the component financial information;
  - (i) Other significant matters that the component auditor communicated or expects to communicate to component management or those charged with governance of the component;
  - (j) Any other matters that may be relevant to the group audit, or that the component auditor determines are appropriate to draw to the attention of the group auditor, including exceptions noted in the written representations that the component auditor requested from component management; and
  - (k) The component auditor's overall findings or conclusions. (Ref: Para. A144)
46. The group auditor shall:
- (a) Discuss significant matters arising from communications with the component auditor, including those in accordance with paragraph 45, with the component auditor, component management or group management, as appropriate; and
  - (b) Evaluate whether communications with the component auditor are adequate for the group auditor's purposes. If such communications are not adequate for the group auditor's purposes, the group auditor shall consider the implications for the group audit. (Ref: Para. A144A)
47. The group auditor shall determine whether, and the extent to which, it is necessary to review additional component auditor audit documentation. In making this determination, the group auditor shall consider: (Ref: Para. A145–A146)
- (a) The nature, timing and extent of the work performed by the component auditor;
  - (b) The competence and capabilities of the component auditor as determined in accordance with paragraph 26(a); and
  - (c) The direction and supervision of the component auditor and review of their work.
48. If the group auditor concludes that the work of the component auditor is not adequate for the group auditor's purposes, the group auditor shall determine what additional audit procedures are to be performed, and whether they are to be performed by a component auditor or by the group auditor.

### **Subsequent Events**

49. In applying ISA 560,<sup>28</sup> the group auditor shall take responsibility for performing procedures, including, as appropriate, requesting component auditors to perform procedures, designed to identify events that may require adjustment of, or disclosure in, the group financial statements. (Ref: Para. A147)

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<sup>28</sup> ISA 560, *Subsequent Events*, paragraphs 6–7

*Considerations When Component Auditors Are Involved*

50. The group auditor shall request the component auditors to notify the group auditor if they become aware of subsequent events that may require adjustment of, or disclosure in, the group financial statements. (Ref: Para. A147)

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

51. In applying ISA 330,<sup>29</sup> the group auditor shall evaluate whether sufficient appropriate audit evidence has been obtained from the audit procedures performed, including from the work performed by component auditors, on which to base the group audit opinion. (Ref: Para. A148–A152)
52. The group engagement partner shall evaluate the effect on the group audit opinion of any uncorrected misstatements (whether identified by the group auditor or communicated by component auditors) and any instances when there has been an inability to obtain sufficient appropriate audit evidence. (Ref: Para. A153)

**Auditor’s Report**

53. The auditor’s report on the group financial statements shall not refer to a component auditor, unless required by law or regulation to include such reference. If such reference is required by law or regulation, the auditor’s report shall indicate that the reference does not diminish the group engagement partner’s or the group engagement partner’s firm’s responsibility for the group audit opinion. (Ref: Para. A154–A155)

**Communication with Group Management and Those Charged with Governance of the Group**

*Communication with Group Management*

54. The group auditor shall communicate with group management an overview of the planned scope and timing of the audit, including an overview of the work to be performed at components of the group. (Ref: Para. A156)
55. If fraud has been identified by the group auditor or brought to its attention by a component auditor (see paragraph 45(h)), or information indicates that a fraud may exist, the group auditor shall communicate this on a timely basis to the appropriate level of group management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities. (Ref: Para. A157)
56. A component auditor may be required by statute, regulation or other reasons to express an audit opinion on the financial statements of an entity or business unit that forms part of the group. In that case, the group auditor shall request group management to inform management of the entity or business unit of any matter of which the group auditor becomes aware that may be significant to the financial statements of the entity or business unit, but of which management of the entity or business unit may be unaware. If group management refuses to communicate the matter to management of the entity or business unit, the group auditor shall discuss the matter with those charged with governance of the group. If the matter remains unresolved, the group auditor, subject to legal and professional confidentiality considerations, shall consider whether to advise the component auditor not to issue the auditor’s report on the financial statements of the entity or business unit until the matter is resolved. (Ref: Para. A158–A159)

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<sup>29</sup> ISA 330, paragraph 26

*Communication with Those Charged with Governance of the Group*

57. The group auditor shall communicate the following matters with those charged with governance of the group, in addition to those required by ISA 260 (Revised)<sup>30</sup> and other ISAs: (Ref: Para. A160)
- (a) An overview of the work to be performed at the components of the group and the nature of the group auditor's planned involvement in the work to be performed by component auditors. (Ref: Para. A161)
  - (b) Instances when the group auditor's review of the work of a component auditor gave rise to a concern about the quality of that component auditor's work, and how the group auditor addressed the concern.
  - (c) Any limitations on the scope of the group audit, for example, significant matters related to restrictions on access to people or information.
  - (d) Fraud or suspected fraud involving group management, component management, employees who have significant roles in the group's system of internal control or others when the fraud resulted in a material misstatement of the group financial statements.

*Communication of Identified Deficiencies in Internal Control*

58. In applying ISA 265,<sup>31</sup> the group auditor shall determine whether any identified deficiencies in the group's system of internal control are required to be communicated to those charged with governance of the group or group management. In making this determination, the group auditor shall consider deficiencies in internal control that have been identified by component auditors and communicated to the group auditor in accordance with paragraph 45(g). (Ref: Para. A162)

**Documentation**

59. In accordance with ISA 230,<sup>32</sup> the audit documentation for a group audit engagement needs to be sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing and extent of audit procedures performed, the evidence obtained, and the conclusions reached with respect to significant matters arising during the group audit. In applying ISA 230,<sup>33</sup> the group auditor shall include in the audit documentation: (Ref: Para. A163–A166, A176–A179)
- (a) Significant matters related to restrictions on access to people or information within the group that were considered before deciding to accept or continue the engagement, or that arose subsequent to acceptance or continuance, and how such matters were addressed.
  - (b) The basis for the group auditor's determination of components for purposes of planning and performing the group audit. (Ref: Para. A167)
  - (c) The basis for the determination of component performance materiality, and the threshold for communicating misstatements in the component financial information to the group auditor.

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<sup>30</sup> ISA 260 (Revised), *Communication with Those Charged with Governance*

<sup>31</sup> ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*

<sup>32</sup> ISA 230, paragraph 8

<sup>33</sup> ISA 230, paragraphs 1–3, 9–11, A6–A7 and Appendix

- (d) The basis for the group auditor’s determination that component auditors have the appropriate competence and capabilities, including sufficient time, to perform the assigned audit procedures at the components. (Ref: Para. A168)
- (e) Key elements of the understanding of the group’s system of internal control in accordance with paragraph 30(c);
- (f) The nature, timing and extent of the group auditor’s direction and supervision of component auditors and the review of their work, including, as applicable, the group auditor’s review of additional component auditor audit documentation in accordance with paragraph 47. (Ref: Para. A169–A175)
- (g) Matters related to communications with component auditors, including:
  - (i) Matters, if any, related to fraud, related parties or going concern communicated in accordance with paragraph 32.
  - (ii) Matters relevant to the group auditor’s conclusion with regard to the group audit, in accordance with paragraph 45, including how the group auditor has addressed significant matters discussed with component auditors, component management or group management.
- (h) The group auditor’s evaluation of, and response to, findings or conclusions of the component auditors about matters that could have a material effect on the group financial statements.

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## Application and Other Explanatory Material

### Scope of this ISA (Ref: Para. 1–2)

- A1. This ISA also deals with the special considerations for the group engagement partner or group auditor, as applicable, in applying the requirements and guidance in ISA 220 (Revised), including for the direction and supervision of component auditors and the review of their work.
- A2. ISQM 1<sup>34</sup> addresses the engagements for which an engagement quality review is required to be performed. ISQM 2<sup>35</sup> deals with the appointment and eligibility of the engagement quality reviewer and the engagement quality reviewer’s responsibilities relating to performing and documenting an engagement quality review, including for a group audit.
- A3. An entity or business unit of a group may also prepare its own group financial statements that incorporate the financial information of those entities or business units it encompasses (that is, a sub-group). This ISA applies to an audit of the group financial statements of such sub-groups performed for statutory, regulatory or other reasons.
- A4. A single legal entity may be organized with more than one business unit, for example, a company with operations in multiple locations, such as a bank with multiple branches. When those business units have characteristics such as separate locations, separate management, or separate information systems (including a separate general ledger) and the financial information is aggregated in preparing the single legal entity’s financial statements, such financial statements meet the definition of group financial statements because they include the financial information

<sup>34</sup> International Standard on Quality Management (ISQM) 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*

<sup>35</sup> ISQM 2, *Engagement Quality Reviews*

of more than one entity or business unit through a consolidation process.

- A5. In some cases, a single legal entity may configure its information system to capture financial information for more than one product or service line for legal or regulatory reporting or other management purposes. In these circumstances, the entity's financial statements are not group financial statements because there is no aggregation of the financial information of more than one entity or business unit through a consolidation process. Further, capturing separate information (e.g., in a sub-ledger) for legal or regulatory reporting or other management purposes does not create separate entities or business units (e.g., divisions) for purposes of this ISA.

*Groups and Components* (Ref: Para. 4–5)

- A6. The group's information system, including its financial reporting process, may or may not be aligned with the group's organizational structure. For example, a group may be organized according to its legal structure, but its information system may be organized by function, process, product or service (or by groups of products or services), or geographic locations for management or reporting purposes.
- A7. Based on the understanding of the group's organizational structure and information system, the group auditor may determine that the financial information of certain entities or business units may be considered together for purposes of planning and performing audit procedures. For example, a group may have three legal entities with similar business characteristics, operating in the same geographical location, under the same management, and using a common system of internal control, including the information system. In these circumstances, the group auditor may decide to treat these three legal entities as one component.
- A8. A group may also centralize activities or processes that are applicable to more than one entity or business unit within the group, for example through the use of a shared service center. When such centralized activities are relevant to the group's financial reporting process, the group auditor may determine that the shared service center is a component.
- A9. Another consideration that may be relevant to the group auditor's determination of components is how management has determined operating segments in accordance with the disclosure requirements of the applicable financial reporting framework.<sup>36</sup>

*Involvement of Component Auditors* (Ref: Para. 6–8)

- A10. Component auditors may perform an audit of the financial statements of a component, whether for statutory, regulatory or other reasons, particularly when a component is a legal entity. When a component auditor is also performing or has completed an audit of the component financial statements, the group auditor may be able to use audit work performed on the component financial statements, provided the group auditor is satisfied that such work is appropriate for purposes of the group audit. In addition, component auditors may adapt the work performed on the audit of the component financial statements to also meet the needs of the group auditor. In any event, the requirements of this ISA apply, including those relating to the direction and supervision of component auditors and the review of their work.
- A10A. In accordance with ISA 220 (Revised),<sup>37</sup> the engagement partner is required to determine that the approach to direction, supervision and review is responsive to the nature and circumstances of the audit engagement. Paragraph A73 provides examples of different ways in which the group

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<sup>36</sup> See, for example, International Financial Reporting Standard (IFRS) 8, *Operating Segments*

<sup>37</sup> ISA 220 (Revised), paragraph 30(b)

engagement partner may take responsibility for directing and supervising component auditors and reviewing their work, and may be helpful in circumstances when the group auditor plans to use the audit work from an audit of component financial statements that has already been completed.

- A11. As explained in ISA 200,<sup>38</sup> detection risk relates to the nature, timing and extent of the auditor's procedures that are determined by the auditor to reduce audit risk to an acceptably low level. Detection risk is a function not only of the effectiveness of an audit procedure but also the application of that procedure by the auditor. Therefore, detection risk is influenced by matters such as adequate planning, the assignment of appropriate resources to the engagement, the exercise of professional skepticism, and the supervision and review of the audit work performed.
- A12. Detection risk is a broader concept than aggregation risk as described in paragraphs 14(a) and A18. In a group audit, there may be a higher probability that the aggregate of uncorrected and undetected misstatements may exceed materiality for the group financial statements as a whole because audit procedures may be performed separately on the financial information of components across the group. Accordingly, component performance materiality is set by the group auditor to reduce aggregation risk to an appropriately low level.

*Professional Skepticism* (Ref: Para. 9)

- A13. ISA 220 (Revised)<sup>39</sup> provides examples of the impediments to the exercise of professional skepticism at the engagement level, including unconscious auditor biases that may impede the exercise of professional skepticism when designing and performing audit procedures and evaluating audit evidence. ISA 220 (Revised) also provides possible actions that the engagement team may take to mitigate impediments to the exercise of professional skepticism at the engagement level.
- A14. Requirements and relevant application material in ISA 315 (Revised 2019),<sup>40</sup> ISA 540 (Revised)<sup>41</sup> and other ISAs address the exercise of professional skepticism, and include examples of how documentation may help provide evidence of the auditor's exercise of professional skepticism.
- A15. All members of the engagement team are required to exercise professional skepticism throughout the group audit. The group auditor's direction and supervision of engagement team members, including component auditors, and the review of their work, may inform the group auditor about whether the engagement team has appropriately exercised professional skepticism.
- A16. The exercise of professional skepticism in a group audit may be affected by matters such as the following:
- Component auditors in different locations may be subject to varying cultural influences, which may affect the nature of the biases to which they are subject.
  - The complex structure of some groups may introduce factors that give rise to increased susceptibility to risks of material misstatement. In addition, an overly complex organizational structure may be a fraud risk factor in accordance with ISA 240<sup>42</sup> and therefore may require additional time or expertise to understand the business purpose and

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<sup>38</sup> ISA 200, paragraph A45

<sup>39</sup> ISA 220 (Revised), paragraphs A34–A36

<sup>40</sup> ISA 315 (Revised 2019), paragraph A238

<sup>41</sup> ISA 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*, paragraph A11

<sup>42</sup> ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, Appendix 1

activities of certain entities or business units.

- The nature and extent of intra-group transactions (e.g., transactions that involve multiple entities and business units within the group or multiple related parties), cash flows or transfer pricing agreements may give rise to additional complexities. In some cases, such matters may also give rise to fraud risk factors.
- When the group audit is subject to tight reporting deadlines imposed by group management, this may put pressure on engagement team members when completing the work assigned. In these circumstances, the engagement team may need to take additional time to appropriately question management's assertions, make appropriate judgments, or appropriately review the audit work performed.

A17. The exercise of professional skepticism by the group auditor includes remaining alert for inconsistent information from component auditors, component management and group management about matters that may be significant to the group financial statements.

### **Definitions**

#### *Aggregation Risk* (Ref: Para. 14(a))

A18. Aggregation risk exists in all audits of financial statements, but is particularly important to understand and address in a group audit because there is a greater likelihood that audit procedures will be performed on classes of transactions, account balances or disclosures that are disaggregated across components. Generally, aggregation risk increases as the number of components increases at which audit procedures are performed separately, whether by component auditors or other members of the engagement team.

#### *Component* (Ref: Para. 14(b))

A19. The group auditor uses professional judgment in determining components at which audit work will be performed. Paragraph A7 explains that the financial information of certain entities or business units may be considered together for purposes of planning and performing audit procedures. However, the group auditor's responsibility for the identification and assessment of the risks of material misstatement of the group financial statements encompasses all of the entities and business units whose financial information is included in the group financial statements.

#### *Component Auditor* (Ref: Para. 14(c))

A20. References in this ISA to the engagement team include the group auditor and component auditors. Component auditors may be from a network firm, a firm that is not a network firm, or the group auditor's firm (e.g., another office within the group auditor's firm).

A21. In some circumstances, the group auditor may perform centralized testing on classes of transactions, account balances or disclosures, or may perform audit procedures related to a component. In these circumstances, the group auditor is not considered a component auditor.

A21A. Paragraph 24 requires the group auditor to request the component auditor to confirm that the component auditor will cooperate with the group auditor and perform the work requested by the group auditor. Paragraph A55 provides guidance for circumstances in which the component auditor is unable to provide such a confirmation.

#### *Component Management* (Ref: Para. 14(d))

A22. Component management refers to management responsible for the financial information or other activity (e.g., processing of transactions at a shared service center) at an entity or business unit that is part of the group. When the group auditor considers the financial information of certain entities or business units together as a component or determines that a shared service center is a component (see paragraphs A7–A8), component management refers to the management that is responsible for the financial information or transaction processing that is subject to the audit procedures being performed in relation to that component. In some circumstances, there may not be separate component management and group management may be directly responsible for the financial information or other activities of the component.

*Group Engagement Partner* (Ref: Para. 14(j))

A23. When joint auditors conduct a group audit, the joint engagement partners and their engagement teams collectively constitute the “group engagement partner” and “engagement team” for the purposes of the ISAs. This ISA does not, however, deal with the relationship between joint auditors or the work that one joint auditor performs in relation to the work of the other joint auditor for purposes of the group audit.

*Group Financial Statements* (Ref: Para. 2, 14(k))

A24. The requirements for the preparation and presentation of the group financial statements may be specified in the applicable financial reporting framework, which may therefore affect the determination of the financial information of entities or business units to be included in the group financial statements. For example, some frameworks require the preparation of consolidated financial statements when an entity (a parent entity) controls one or more other entities (e.g., subsidiaries) through majority ownership interest or other means. In some cases, the applicable financial reporting framework includes separate requirements for, or may otherwise permit, the presentation of combined financial statements. Examples of circumstances in which the presentation of combined financial statements may be permitted include entities that have no parent but are under common control or entities under common management.

A25. The term “consolidation process” as used in this ISA is not intended to have the same meaning as “consolidation” or “consolidated financial statements” as defined or described in financial reporting frameworks. Rather, the term “consolidation process” refers more broadly to the process used to prepare group financial statements.

A26. The detailed aspects of the consolidation process vary from one group to another, depending on the group’s structure and information system, including the financial reporting process. However, a consolidation process involves considerations such as the elimination of intra-group transactions and balances and, when applicable, implications of different reporting periods for entities or business units included in the group financial statements.

**Leadership Responsibilities for Managing and Achieving Quality on a Group Audit** (Ref: Para. 11, 16)

- A27. It may not be possible or practical for the group engagement partner to solely deal with all requirements in ISA 220 (Revised), particularly when the engagement team includes a large number of component auditors located in multiple locations. In managing quality at the engagement level, ISA 220 (Revised)<sup>43</sup> permits the engagement partner to assign the design or performance of procedures, tasks or actions to other members of the engagement team to assist the engagement partner. Accordingly, the group engagement partner may assign procedures, tasks or actions to other members of the engagement team and these members may assign procedures, tasks or actions further. In such circumstances, ISA 220 (Revised) requires that the engagement partner shall continue to take overall responsibility for managing and achieving quality on the audit engagement.
- A28. Policies or procedures established by the firm, or that are common network requirements or network services,<sup>44</sup> may support the group engagement partner by facilitating communication between the group auditor and component auditors and supporting the group auditor's direction and supervision of those component auditors and the review of their work.
- A29. ISA 220 (Revised)<sup>45</sup> explains that a culture that demonstrates a commitment to quality is shaped and reinforced by the engagement team members as they demonstrate expected behaviors when performing the engagement. In addressing the requirement in paragraph 16(a), the group engagement partner may communicate directly to other members of the engagement team (including component auditors) and reinforce this communication through personal conduct and actions (e.g., leading by example).

**Acceptance and Continuance**

*Determining Whether Sufficient and Appropriate Audit Evidence Can Reasonably Be Expected to Be Obtained* (Ref: Para. 17–18)

- A30. In determining whether sufficient appropriate audit evidence can reasonably be expected to be obtained, the group engagement partner may obtain an understanding of matters such as:
- The group structure, including both the legal and organizational structure.
  - Activities that are significant to the group, including the industry and regulatory, economic and political environments in which those activities take place.
  - The use of service organizations.
  - The use of shared service centers.
  - The consolidation process.
  - Whether the group auditor:
    - Will have unrestricted access to those charged with governance of the group, group management, those charged with governance of the component, component management and component information, including of those components that are accounted for by the equity method; and

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<sup>43</sup> ISA 220 (Revised), paragraph 15

<sup>44</sup> ISQM 1, paragraphs 48–52

<sup>45</sup> ISA 220 (Revised), paragraph A28

- Will be able to perform necessary work on the financial information of the components when applicable.
  - Whether sufficient and appropriate resources are assigned or will be made available.
- A31. In the case of an initial group audit engagement, the group auditor's understanding of the matters in paragraph A30 may be obtained from:
- Information provided by group management;
  - Communication with group management;
  - Communication with those charged with governance of the group; and
  - When applicable, communication with component management or the predecessor auditor.
- A32. For a recurring engagement, the ability to obtain sufficient appropriate audit evidence may be affected by significant changes, for example, changes in:
- The group structure (e.g., acquisitions, disposals, joint ventures, reorganizations, or changes in how the group financial reporting system is organized).
  - Components' activities that are significant to the group.
  - The composition of those charged with governance of the group, group management, or key management of components for which audit procedures are expected to be performed.
  - The group auditor's understanding of the integrity and competence of group or component management.
  - The applicable financial reporting framework.
- A33. There may be additional complexities with obtaining sufficient appropriate audit evidence in a group audit when components are located in jurisdictions other than the group auditor's jurisdiction because of cultural and language differences, and different laws or regulations. For example, law or regulation may restrict the component auditor from providing documentation outside of its jurisdiction, or war, civil unrest or outbreaks of disease may restrict the group auditor's access to relevant component auditor audit documentation. Paragraph A177 includes possible ways to address these situations.
- A34. Restrictions may be imposed after the group engagement partner's acceptance of the group audit engagement that may affect the engagement team's ability to obtain sufficient appropriate audit evidence. Such restrictions may include those affecting:
- The group auditor's access to component information, management or those charged with governance of components, or the component auditors (including relevant audit documentation sought by the group auditor) (see paragraphs 20 and 21); or
  - The work to be performed on the financial information of components.

Paragraphs A42–A43 explain the possible effect of such restrictions on the auditor's report on the group financial statements.

*Agreeing the Terms of Audit Engagements* (Ref: Para. 19)

A35. ISA 210<sup>46</sup> requires the auditor to agree the terms of the audit engagement with management or

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<sup>46</sup> ISA 210, paragraph 9 and 10(d)

those charged with governance, as appropriate. The terms of engagement identify the applicable financial reporting framework. Additional matters that may be included in the terms of a group audit engagement include:

- Communications between the group auditor and component auditors should be unrestricted to the extent possible under laws or regulations;
- Important communications between component auditors and those charged with governance of the component or component management, including communications on significant deficiencies in internal control, should be communicated to the group auditor;
- Communications between regulatory authorities and entities or business units related to financial reporting matters that may be relevant to the group audit should be communicated to the group auditor; and
- The group auditor should be permitted to perform work, or request a component auditor to perform work, at the component.

*Restrictions on Access to Information or People (Ref: Para. 20–21)*

A36. Restrictions on access to information or people do not eliminate the requirement for the group auditor to obtain sufficient appropriate audit evidence.

A37. Access to information or people can be restricted for many reasons, such as restrictions imposed by component management, laws or regulations or other conditions, for example, war, civil unrest or outbreaks of disease. Paragraph A177 describes how the group auditor may be able to overcome restrictions on access to component auditor audit documentation.

A38. In some circumstances, the group auditor may be able to overcome restrictions on access to information or people, for example:

- If access to component management or those charged with governance of the component is restricted, the group auditor may request group management or those charged with governance of the group to assist with removing the restriction or otherwise request information directly from group management or those charged with governance of the group.
- If the group has a non-controlling interest in an entity that is accounted for by the equity method, the group auditor may determine whether provisions exist (e.g., in the terms of joint venture agreements, or the terms of other investment agreements) regarding access by the group to the financial information of the entity and request group management to exercise such rights.
- If the group has a non-controlling interest in an entity that is accounted for by the equity method and the group has representatives who are on the executive board or are members of those charged with governance of the non-controlled entity, the group auditor may inquire whether they can provide financial and other information available to them in these roles.

A39. If the group has a non-controlling interest in an entity that is accounted for by the equity method and the group auditor's access to information or people at the entity is restricted, the group auditor may be able to obtain information to be used as audit evidence regarding the entity's financial information, for example:

- Financial information that is available from group management, as group management also needs to obtain the non-controlled entity's financial information in order to prepare the

group financial statements.

- Publicly available information, such as audited financial statements, public disclosure documents, or quoted prices of equity instruments in the non-controlled entity.

It is a matter of professional judgment, particularly in view of the assessed risks of material misstatement of the group financial statements and considering other sources of information that may corroborate or otherwise contribute to audit evidence obtained, whether the auditor can obtain sufficient appropriate audit evidence.<sup>47</sup>

A39A. If the group has a non-controlling interest in an entity that is accounted for by the equity method and access to information or people at the entity is restricted, the group auditor may consider whether such restrictions are inconsistent with group management's assertions regarding the appropriateness of the use of the equity method of accounting.

A40. When the group auditor is unable to obtain sufficient appropriate audit evidence due to restrictions on access to information or people, the group auditor may:

- Communicate the restrictions to the group auditor's firm to assist the group auditor in determining an appropriate course of action. For example, the group auditor's firm may communicate with group management about the restrictions and encourage group management to communicate with regulators. This may be useful when restrictions affect multiple audits in the jurisdiction or by the same firm, for example, because of war, civil unrest or outbreaks of disease in a major economy.
- Be required by law or regulation to communicate with regulators, listing authorities, or others, about the restrictions.

A41. Restrictions on access may have other implications for the group audit. For example, if restrictions are imposed by group management, the group auditor may need to reconsider the reliability of group management's responses to the group auditor's inquiries and whether the restrictions call into question group management's integrity.

#### *Effect of Restrictions on Access to Information or People on the Auditor's Report on Group Financial Statements*

A42. ISA 705 (Revised)<sup>48</sup> contains requirements and guidance about how to address situations when the group auditor is unable to obtain sufficient appropriate audit evidence. Appendix 1 contains an example of an auditor's report containing a qualified group audit opinion based on the group auditor's inability to obtain sufficient appropriate audit evidence in relation to a component that is accounted for by the equity method.

#### *Law or Regulation Prohibit the Group Engagement Partner from Declining or Withdrawing from an Engagement*

A43. Law or regulation may prohibit the group engagement partner from declining or withdrawing from an engagement. For example, in some jurisdictions the auditor is appointed for a specified period of time and is prohibited from withdrawing before the end of that period. Also, in the public sector, the option of declining or withdrawing from an engagement may not be available to the auditor due to the nature of the mandate or public interest considerations. In these circumstances, the requirements in this ISA still apply to the group audit, and the effect of the group auditor's inability

<sup>47</sup> ISA 330, paragraph 7(b)

<sup>48</sup> ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

to obtain sufficient appropriate audit evidence is addressed in ISA 705 (Revised).

### **Overall Group Audit Strategy and Group Audit Plan**

#### *The Continual and Iterative Nature of Planning and Performing a Group Audit (Ref: Para. 22)*

A44. As explained in ISA 300,<sup>49</sup> planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement. For example, due to unexpected events, changes in conditions, or audit evidence obtained from risk assessment or further audit procedures, the group auditor may need to modify the overall group audit strategy and group audit plan, and the resulting planned nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks. The group auditor may also modify the determination of the components at which to perform audit work as well as the nature, timing and extent of the component auditors' involvement. ISA 300<sup>50</sup> requires the auditor to update and change the overall audit strategy and audit plan as necessary during the course of the audit.

#### *Establishing the Overall Group Audit Strategy and Group Audit Plan (Ref: Para. 22)*

A45. In an initial group audit engagement, the group auditor may have a preliminary understanding of the group and its environment, the applicable financial reporting framework and the entity's system of internal control based on information obtained from group management, those charged with governance of the group and, when applicable, communication with component management or the predecessor auditor. In a recurring group audit engagement, the group auditor's preliminary understanding may be obtained through prior period audits. This preliminary understanding may assist the group auditor in developing initial expectations about the classes of transactions, account balances and disclosures that may be significant.

A46. The group auditor may also use information obtained during the engagement acceptance and continuance process in establishing the overall group audit strategy and group audit plan, for example, in relation to the resources needed to perform the group audit.

A47. The process of establishing the overall group audit strategy and group audit plan and initial expectations about the classes of transactions, account balances and disclosures that may be significant at the group financial statement level may assist the group auditor in developing a preliminary determination of matters such as:

- Whether to perform audit work centrally, at components or a combination thereof; and
- The nature, timing and extent of audit work to be performed with respect to the financial information of components (e.g., design and perform risk assessment procedures, further audit procedures, or a combination thereof).

#### *Components at Which to Perform Audit Work (Ref: Para. 22(a))*

A48. The determination of components at which to perform audit work is a matter of professional judgment. Matters that may influence the group auditor's determination include, for example:

- The nature of events or conditions that may give rise to risks of material misstatement at the assertion level of the group financial statements that are associated with a component,

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<sup>49</sup> ISA 300, paragraph A2

<sup>50</sup> ISA 300, paragraph 10

for example:

- Newly formed or acquired entities or business units.
  - Entities or business units in which significant changes have taken place.
  - Significant transactions with related parties.
  - Significant transactions outside the normal course of business.
  - Abnormal fluctuations identified by analytical procedures performed at the group level, in accordance with ISA 315 (Revised 2019).<sup>51</sup>
- The disaggregation of significant classes of transactions, account balances and disclosures in the group financial statements across components, considering the size and nature of assets, liabilities and transactions at the location or business unit relative to the group financial statements.
  - Whether sufficient appropriate audit evidence is expected to be obtained for all significant classes of transactions, account balances and disclosures in the group financial statements from audit work planned on the financial information of identified components.
  - The nature and extent of misstatements or control deficiencies identified at a component in prior period audits.
  - The nature and extent of the commonality of controls across the group and whether, and if so, how, the group centralizes activities relevant to financial reporting.

*Resources* (Ref: Para. 22(b))

A49. Matters that influence the group auditor's determination of the resources needed to perform the group audit and the nature, timing and extent to which component auditors are to be involved are a matter of professional judgment and may include, for example:

- The understanding of the group, the components within the group at which audit work is to be performed and whether to perform work centrally, at components or a combination thereof.
- The knowledge and experience of the engagement team. For example, component auditors may have greater experience and a more in-depth knowledge than the group auditor of the local industries in which components operate, local laws or regulations, business practices, language and culture. In addition, the involvement of auditor's experts may be needed on complex matters.
- The initial expectations about the potential risks of material misstatement.
- The amount or location of resources to allocate to specific audit areas. For example, the extent to which components are dispersed across multiple locations may impact the need to involve component auditors in specific locations.
- Access arrangements. For example, when the group auditor's access to a component in a particular jurisdiction is restricted, component auditors may need to be involved.
- The nature of the components' activities, including their complexity or specialization of operations.
- The group's system of internal control, including the information system in place, and its

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<sup>51</sup> ISA 315 (Revised 2019), paragraph 14(b)

degree of centralization. For example, the involvement of component auditors may be more likely when the system of internal control is decentralized.

- Previous experience with the component auditor.
- A50. Component auditors may be involved in different phases of an audit, for example, component auditors may design or perform:
- Risk assessment procedures; and
  - Procedures to respond to the assessed risks of material misstatement.
- A51. The nature, timing and extent to which component auditors are to be involved depends on the facts and circumstances of the group audit engagement. Often component auditors will be involved in all phases of the audit, but the group auditor may decide to involve component auditors only in a certain phase. When the group auditor does not intend to involve component auditors in risk assessment procedures, the group auditor may still discuss with component auditors whether there are any significant changes in the business or the system of internal control of the component that could have an effect on the risks of material misstatement of the group financial statements.
- A52. ISA 300<sup>52</sup> requires the engagement partner and other key members of the engagement team to be involved in planning the audit. When component auditors are involved, one or more individuals from a component auditor may be key members of the engagement team and therefore involved in planning the group audit. The involvement of component auditors in planning the audit draws on their experience and insight, thereby enhancing the effectiveness and efficiency of the planning process. The group engagement partner uses professional judgment in determining which component auditors to involve in planning the audit. This may be affected by the nature, timing and extent to which the component auditors are expected to be involved in designing and performing risk assessment or further audit procedures.
- A53. As described in ISQM 1,<sup>53</sup> there may be circumstances when the fee quoted for an engagement is not sufficient given the nature and circumstances of the engagement, and it may diminish the firm's ability to perform the engagement in accordance with professional standards and applicable legal or regulatory requirements. The level of fees, including their allocation to component auditors, and the extent to which they relate to the resources required may be a special consideration for group audit engagements. For example, in a group audit, the firm's financial and operational priorities may place constraints on the determination of the components at which audit work will be performed, as well as the resources needed, including the involvement of component auditors. In such circumstances, these constraints do not override the group engagement partner's responsibility for achieving quality at the engagement level or the requirements for the group auditor to obtain sufficient appropriate audit evidence on which to base the group audit opinion.

#### *Considerations When Component Auditors Are Involved*

##### Sufficient and Appropriate Involvement in the Work of the Component Auditor (Ref: Para. 23–24)

- A54. In evaluating whether the group auditor will be able to be sufficiently and appropriately involved in the work of the component auditor, the group auditor may obtain an understanding of whether the component auditor is subject to any restrictions that limit communication with the group

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<sup>52</sup> ISA 300, paragraph 5

<sup>53</sup> ISQM 1, paragraph A74

auditor, including with regard to sharing audit documentation with the group auditor. The group auditor may also obtain an understanding about whether audit evidence related to components located in a different jurisdiction may be in a different language and may need to be translated for use by the group auditor.

A55. If the component auditor is unable to cooperate with the group auditor, the group auditor may:

- Request the component auditor to provide its rationale.
- Be able to take appropriate action to address the matter, including adjusting the nature of the work requested to be performed. Alternatively, in accordance with paragraph 27, the group auditor may need to obtain sufficient appropriate audit evidence relating to the work to be performed at the component without involving the component auditor.

Relevant Ethical Requirements, Including Those Related to Independence (Ref: Para. 25)

A56. When performing work at a component for a group audit engagement, the component auditor is subject to ethical requirements, including those related to independence, that are relevant to the group audit engagement. Such requirements may be different from or in addition to those applying to the component auditor when performing an audit on the financial statements of an entity or business unit that is part of the group for statutory, regulatory or other reasons in the component auditor's jurisdiction.

A57. In making the component auditors aware of relevant ethical requirements, the group auditor may consider whether additional information or training for component auditors is necessary regarding the provisions of the ethical requirements that are relevant to the group audit engagement.

Engagement Resources (Ref: Para. 26)

A58. ISA 220 (Revised)<sup>54</sup> requires the engagement partner to determine that sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team in a timely manner. When sufficient or appropriate resources are not made available in relation to work to be performed by a component auditor, the group engagement partner may discuss the matter with the component auditor, group management or the group auditor's firm and may subsequently request the component auditor or the group auditor's firm to make sufficient and appropriate resources available.

Competence and capabilities of the component auditors

A59. ISA 220 (Revised)<sup>55</sup> provides guidance regarding matters the engagement partner may take into consideration when determining the competence and capabilities of the engagement team. This determination is particularly important in a group audit when the engagement team includes component auditors. ISA 220 (Revised)<sup>56</sup> indicates that the firm's policies or procedures may require the firm or the engagement partner to take different actions from those applicable to personnel when obtaining an understanding of whether a component auditor from another firm has the appropriate competence and capabilities to perform the audit engagement.

A60. Determining whether component auditors have the appropriate competence and capabilities is a matter of professional judgment and is influenced by the nature and circumstances of the group audit engagement. This determination influences the nature, timing and extent of the group

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<sup>54</sup> ISA 220 (Revised), paragraph 25

<sup>55</sup> ISA 220 (Revised), paragraph A71

<sup>56</sup> ISA 220 (Revised), paragraph A24

engagement partner's direction and supervision of the component auditor and the review of their work.

A61. In determining whether component auditors have the appropriate competence and capabilities to perform the assigned audit procedures at the component, the group engagement partner may consider matters such as:

- Previous experience with or knowledge of the component auditor.
- The component auditor's specialized skills (e.g., industry-specific knowledge).
- The degree to which the group auditor and component auditor are subject to a common system of quality management, for example, whether the group auditor and a component auditor:
  - Use common resources to perform the work (e.g., audit methodologies or information technology (IT) applications);
  - Share common policies or procedures affecting engagement performance (e.g., direction, supervision and review of work or consultation);
  - Are subject to common monitoring activities; or
  - Have other commonalities, including common leadership or a common cultural environment.
- The consistency or similarity of:
  - Laws or regulations or legal system;
  - Language and culture;
  - Education and training;
  - Professional oversight, discipline, and external quality assurance; or
  - Professional organizations and standards.
- Information obtained about the component auditor through interactions with component management, those charged with governance, and other key personnel, such as internal auditors.

A62. The procedures to determine the component auditor's competency and capability may include, for example:

- An evaluation of the information communicated by the group auditor's firm to the group auditor, including:
  - The firm's ongoing communication related to monitoring and remediation, in circumstances when the group auditor and component auditor are from the same firm.<sup>57</sup>
  - Information from the network about the results of the monitoring activities undertaken by the network across the network firms.<sup>58</sup>
  - Information obtained from professional body(ies) to which the component auditor belongs, the authorities by which the component auditor is licensed, or other third

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<sup>57</sup> ISQM 1, paragraph 47

<sup>58</sup> ISQM 1, paragraph 51(b)

parties.

- Discussing the assessed risks of material misstatement with the component auditor.
- Requesting the component auditor to confirm their understanding of the matters referred to in paragraph 25 in writing.
- Discussing the component auditor's competence and capabilities with colleagues in the group engagement partner's firm that have worked directly with the component auditor.
- Obtaining published external inspection reports.

A63. The group engagement partner's firm and the component auditor may be members of the same network and may be subject to common network requirements or use common network services.<sup>59</sup> When determining whether component auditors have the appropriate competence and capabilities to perform work in support of the group audit engagement, the group engagement partner may be able to depend on such network requirements, for example, those addressing professional training, or recruitment or that require the use of audit methodologies and related implementation tools. In accordance with ISQM 1,<sup>60</sup> the firm is responsible for designing, implementing and operating its system of quality management, and the firm may need to adapt or supplement network requirements or network services to be appropriate for use in its system of quality management.

Using the work of an auditor's expert

A64. ISA 220 (Revised)<sup>61</sup> requires the engagement partner to determine that members of the engagement team, and any auditor's external experts who are not part of the engagement team, collectively have the appropriate competence and capabilities, including sufficient time, to perform the audit engagement. If an auditor's expert is used by a component auditor, the group engagement partner may need to obtain information from the component auditor. For example, the group auditor may discuss with the component auditor, the component auditor's evaluation of the competence and capabilities of the auditor's expert.

Automated tools and techniques

A65. When determining whether the engagement team has the appropriate competence and capabilities, the group engagement partner may take into consideration such matters as the expertise of the component auditor in the use of automated tools and techniques. For example, as described in ISA 220 (Revised),<sup>62</sup> when the group auditor requires component auditors to use specific automated tools and techniques when performing audit procedures, the group auditor may communicate with component auditors that the use of such automated tools and techniques need to comply with the group auditor's instructions.

Application of the Group Auditor's Understanding of a Component Auditor (Ref: Para. 27)

A66. ISA 220 (Revised)<sup>63</sup> requires the engagement partner to take responsibility for other members of the engagement team having been made aware of relevant ethical requirements that are applicable given the nature and circumstances of the audit engagement, and the firm's related

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<sup>59</sup> ISQM 1, paragraphs A19, A175

<sup>60</sup> ISQM 1, paragraph 48–49

<sup>61</sup> ISA 220 (Revised), paragraph 26

<sup>62</sup> ISA 220 (Revised), paragraph A65

<sup>63</sup> ISA 220 (Revised), paragraph 17

policies or procedures. This includes the firm's policies or procedures that address circumstances that may cause a breach of relevant ethical requirements, including those related to independence, and the responsibilities of members of the engagement team when they become aware of breaches. The firm's policies or procedures also may address breaches of independence requirements by component auditors, and actions the group auditor may take in those circumstances in accordance with the relevant ethical requirements. In addition, relevant ethical requirements or law or regulation may also specify particular communications to those charged with governance in circumstances when breaches of independence requirements have been identified.<sup>64</sup>

- A67. If there has been a breach by a component auditor of the relevant ethical requirements that apply to the group audit engagement, including those related to independence, and the breach has not been satisfactorily addressed in accordance with provisions of the relevant ethical requirements, the group auditor cannot use the work of that component auditor.
- A68. Serious concerns are those concerns that in the group auditor's professional judgment cannot be overcome. The group engagement partner may be able to overcome less than serious concerns about the component auditor's professional competency (e.g., lack of industry-specific knowledge), or the fact that the component auditor does not operate in an environment that actively oversees auditors, by the group auditor being more involved in the work of the component auditor or by directly performing further audit procedures on the financial information of the component.

#### Engagement Performance (Ref: Para. 28)

- A69. ISA 220 (Revised)<sup>65</sup> requires the engagement partner to determine that the nature, timing and extent of direction, supervision and review is planned and performed in accordance with the firm's policies or procedures, professional standards and applicable legal and regulatory requirements, and is responsive to the nature and circumstances of the audit engagement and the resources assigned or made available to the engagement team. For a group audit, the approach to direction, supervision and review will generally include a combination of addressing the group auditor's firm policies or procedures and group audit engagement specific responses.
- A70. For a group audit, particularly when the engagement team includes a large number of component auditors that may be located in multiple locations, the group engagement partner may assign the design or performance of procedures, tasks or actions to other members of the engagement team to assist the group engagement partner in fulfilling the responsibility for the nature, timing and extent of the direction and supervision of component auditors and the review of their work (see also paragraph 11).
- A71. If component auditors are from a firm other than the group auditor's firm, the firm's policies or procedures may be different, or different actions may need to be taken, respectively, in relation to the nature, timing and extent of direction and supervision of those members of the engagement team, and the review of their work. In particular, firm policies or procedures may require the firm or the group engagement partner to take different actions from those applicable to members of the engagement team within the firm or the network (e.g., in relation to the form, content and timing of communications with component auditors, including the use of group auditor instructions to component auditors). ISA 220 (Revised) provides examples of actions that may need to be

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<sup>64</sup> ISA 260 (Revised), paragraph A31

<sup>65</sup> ISA 220 (Revised), paragraph 30

taken in such circumstances.<sup>66</sup>

A72. The nature, timing and extent of direction and supervision of component auditors and review of their work may be tailored based on the nature and circumstances of the engagement and, for example:

- The assessed risks of material misstatement. For example, if the group auditor has identified a component that includes a significant risk, an increase in the extent of direction and supervision of the component auditor and a more detailed review of the component auditor's audit documentation may be appropriate.
- The competence and capabilities of the component auditors performing the audit work. For example, if the group auditor has no previous experience working with a component auditor, the group auditor may communicate more detailed instructions, increase the frequency of discussions or other interactions with the component auditor, or assign more experienced individuals to oversee the component auditor as the work is performed.
- The location of engagement team members, including the extent to which engagement team members are dispersed across multiple locations, including when service delivery centers are used.
- Access to component auditor audit documentation. For example, when law or regulation precludes component auditor audit documentation from being transferred out of the component auditor's jurisdiction, the group auditor may be able to review the audit documentation at the component auditor's location or remotely through the use of technology, when not prohibited by law or regulation (see also paragraphs A176–A177).

A73. There are different ways in which the group engagement partner may take responsibility for directing and supervising component auditors and reviewing their work, for example:

- Communications with component auditors throughout the course of the group audit, including communications required by this ISA;
- Meetings or calls with component auditors to discuss identified and assessed risks, issues, findings and conclusions.
- Reviews of the component auditor's audit documentation in person or remotely when permitted by law and regulation.
- Participating in the closing or other key meetings between the component auditors and component management.

A74. In applying ISA 220 (Revised),<sup>67</sup> the group engagement partner is required to review audit documentation at appropriate points in time during the audit engagement, including audit documentation relevant to the group audit relating to:

- Significant matters;
- Significant judgments, including those relating to difficult or contentious matters identified during the audit engagement, and the conclusions reached; and
- Other matters that, in the engagement partner's professional judgment, are relevant to the engagement partner's responsibilities.

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<sup>66</sup> ISA 220 (Revised), paragraph A24–A25

<sup>67</sup> ISA 220 (Revised), paragraphs 31, A92–A93

The review of such audit documentation by the group engagement partner often takes place during the course of the group audit, including the review of relevant component auditor audit documentation (also see paragraph A145).

*Communications with Component Auditors* (Ref: Para. 29)

- A75. Clear and timely communication between the group auditor and the component auditors about their respective responsibilities, along with clear direction to the component auditors about the nature, timing and extent of the work to be performed and the matters expected to be communicated to the group auditor, helps establish the basis for effective two-way communication. Effective two-way communication between the group auditor and the component auditors also helps to set expectations for component auditors and facilitates the group auditor's direction and supervision of them and the review of their work. Such communication also provides an opportunity for the group engagement partner to reinforce the need for component auditors to exercise professional skepticism in the work performed for purposes of the group audit.
- A76. Other factors that may also contribute to effective two-way communication include:
- Clarity of the instructions to the component auditor, particularly when the component auditor is from another firm and may not be familiar with the policies or procedures of the group auditor's firm.
  - A mutual understanding that the component auditor may discuss the audit work requested to be performed, based on the component auditor's knowledge and understanding of the component.
  - A mutual understanding of relevant issues and the expected actions arising from the communication process.
  - The form of communications. For example, matters that need timely attention may be more appropriately discussed in a meeting rather than by exchanging emails.
  - A mutual understanding of the person(s) from the group auditor and component auditors who have responsibility for managing communications regarding particular matters.
  - The process for the component auditor to take action and report back on matters communicated by the group auditor.
- A77. The communications between the group auditor and component auditors depend on the facts and circumstances of the group audit engagement, including the nature and extent of involvement of the component auditors and the degree to which the group auditor and component auditors are subject to common systems of quality management or common network requirements or network services.

Form of communications

- A78. The form of the communications between the group auditor and component auditors may vary based on factors such as the nature of the audit work the component auditors have been requested to perform, and the extent to which communication capabilities are integrated into the audit tools used for the group audit.
- A79. The form of communications also may be affected by such factors as:
- The significance, complexity or urgency of the matter.
  - Whether the matter has been or is expected to be communicated to group management

and those charged with governance of the group.

- A80. Communication between the group auditor and the component auditor may not necessarily be in writing. However, the group auditor's verbal communications with the component auditors may be supplemented by written communication, such as a set of instructions regarding the work to be performed, when the group auditor wants to give particular attention to, or promote a mutual understanding about, certain matters. In addition, the group auditor may meet with the component auditor to discuss significant matters or to review relevant parts of the component auditor's audit documentation.
- A81. Paragraph 45 requires the group auditor to request the component auditor to communicate matters relevant to the group auditor's conclusion with regard to the group audit. As explained in paragraph A144, the form and content of the component auditor's deliverables are influenced by the nature and extent of the audit work the component auditor has been requested to perform.
- A82. Regardless of the form of communication, the documentation requirements of this and other ISAs apply.

#### Timing of communications

- A83. The appropriate timing of communications will vary with the circumstances of the engagement. Relevant circumstances may include the nature, timing and extent of work to be performed by the component auditor and the action expected to be taken by the component auditor. For example, communications regarding planning matters may often be made early in the audit engagement and, for an initial group audit, may be made as part of agreeing the terms of the engagement.

#### Non-compliance with laws or regulations (Ref: Para. 25, 29)

- A84. In applying ISA 250 (Revised),<sup>68</sup> the group engagement partner may become aware of information about non-compliance or suspected non-compliance with laws or regulations. In such circumstances, the group engagement partner may have an obligation under relevant ethical requirements, laws or regulations, to communicate the matter to the component auditor.<sup>69</sup> The obligation of the group engagement partner to communicate non-compliance or suspected non-compliance may extend to auditors of the financial statements of entities or business units for which an audit is required by statute, regulation or for another reason, but for which no audit work is performed for purposes of the group audit.

#### **Understanding the Group and Its Environment, the Applicable Financial Reporting Framework and the Group's System of Internal Control (Ref: Para. 30)**

- A85. ISA 315 (Revised 2019)<sup>70</sup> contains requirements and guidance regarding the auditor's responsibility to obtain an understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control. Appendix 2 of this ISA provides examples of matters related to internal control that may be helpful in obtaining an understanding of the system of internal control in the context of a group environment, and expands on how ISA 315 (Revised 2019) is to be applied to an audit of group financial statements.

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<sup>68</sup> ISA 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*

<sup>69</sup> See, for example, Paragraphs R360.17 and R360.18 of the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code)

<sup>70</sup> ISA 315 (Revised 2019), paragraphs 19–27, A50–A183

- A86. The understanding of the group and its environment, the applicable financial reporting framework, and the group's system of internal control may be obtained through communications with:
- Group management, component management or other appropriate individuals within the entity, including individuals within the internal audit function (if the function exists) and individuals who have knowledge of the group's system of internal control, accounting policies and practices, and the consolidation process;
  - Component auditors; or
  - Auditors that perform an audit for statutory, regulatory or other reasons of the financial statements of an entity or business unit that is part of the group.
- A87. Obtaining an understanding of the group, identifying risks of material misstatement and assessing inherent risk and control risk may be performed in different ways depending on preferred audit techniques or methodologies and may be expressed in different ways. Accordingly, when component auditors are involved in the design and performance of risk assessment procedures, the group auditor may need to communicate its preferred approach with component auditors or provide instructions.

*Engagement Team Discussion* (Ref: Para. 30)

- A88. In applying ISA 315 (Revised 2019),<sup>71</sup> the group engagement partner and other key engagement team members are required to discuss the application of the applicable financial reporting framework and the susceptibility of the group's financial statements to material misstatement. The group engagement partner's determination of which members of the engagement team to include in the discussion and the topics to be discussed, is affected by matters such as initial expectations about the risks of material misstatement and the preliminary expectation of whether to involve component auditors.
- A89. The discussion provides an opportunity to:
- Share knowledge of the components and their environments, including which components' activities are centralized.
  - Exchange information about the business risks of the components or the group, and how inherent risk factors may affect susceptibility to misstatement of classes of transactions, account balances and disclosures.
  - Exchange ideas about how and where the group financial statements may be susceptible to material misstatement due to fraud or error. ISA 240<sup>72</sup> requires the engagement team discussion to place particular emphasis on how and where the entity's financial statements may be susceptible to material misstatement due to fraud, including how fraud may occur.
  - Identify policies followed by group or component management that may be biased or designed to manage earnings that could lead to fraudulent financial reporting.
  - Consider known external and internal factors affecting the group that may create an incentive or pressure for group management, component management, or others to commit fraud, provide the opportunity for fraud to be perpetrated, or indicate a culture or environment that enables group management, component management, or others to rationalize committing fraud.

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<sup>71</sup> ISA 315 (Revised 2019), paragraph 17

<sup>72</sup> ISA 240, paragraph 16

- Consider the risk that group or component management may override controls.
- Discuss fraud that has been identified, or information that indicates existence of a fraud.
- Identify risks of material misstatement relevant to components where there may be impediments to the exercise of professional skepticism.
- Consider whether uniform accounting policies are used to prepare the financial information of the components for the group financial statements and, if not, how differences in accounting policies are identified and adjusted (when required by the applicable financial reporting framework).
- Share information about risks of material misstatement of the financial information of a component that may apply more broadly to some, or all, of the other components.
- Share information that may indicate non-compliance with national laws or regulations, for example, payments of bribes and improper transfer pricing practices.
- Discuss events or conditions identified by group management, component management or the engagement team, that may cast significant doubt on the group's ability to continue as a going concern.
- Discuss related party relationships or transactions identified by group management or component management, and any other related parties of which the engagement team is aware.

*The Group and Its Environment* (Ref: Para. 30 (a))

A90. An understanding of the group's organizational structure and its business model may enable the group auditor to understand such matters as:

- The complexity of the group's structure. A group may be more complex than a single entity because a group may have several subsidiaries, divisions or other business units, including in multiple locations. Also, a group's legal structure may be different from the operating structure, for example, for tax purposes. Complex structures often introduce factors that may give rise to increased susceptibility to material misstatements, such as whether goodwill, joint ventures or special purpose entities are accounted for appropriately and whether adequate disclosures have been made.
- The geographic locations of the group's operations. Having a group that is located in multiple geographical locations may give rise to increased susceptibility to material misstatements. For example, different geographical locations may involve different languages, cultures and business practices.
- The structure and complexity of the group's IT environment. A complex IT environment often introduces factors that may give rise to increased susceptibility to material misstatements. For example, a group may have a complex IT environment because of multiple IT systems that are not integrated due to recent acquisitions or mergers. Therefore, it may be particularly important to obtain an understanding of the complexity of the security over the IT environment, including vulnerability of the IT applications, databases, and other aspects of the IT environment. A group may also use one or more external service providers for aspects of its IT environment.
- Relevant regulatory factors, including the regulatory environment. Different laws or regulations may introduce factors that may give rise to increased susceptibility to material misstatements. A group may have operations that are subject to a high degree of complex

laws or regulations in multiple jurisdictions, or entities or business units in the group that operate in multiple industries that are subject to different types of laws or regulations.

- The ownership, and relationships between owners and other people or entities, including related parties. Understanding the ownership and relationships can be more complex in a group that operates across multiple jurisdictions and when there are changes in ownership through formation, acquisition, disposal or joint venture. These factors may give rise to increased susceptibility to material misstatements.
- A91. Obtaining an understanding of the degree to which the group's operations or activities are similar may help to identify similar risks of material misstatement across components and design an appropriate response.
- A92. The financial results of entities or business units are ordinarily measured and reviewed by group management. Inquiries of group management may reveal that group management relies on certain key indicators to evaluate the financial performance of the group's entities and business units and take action. The understanding of such performance measures may help to identify:
- Areas where there is increased susceptibility to material misstatements (e.g., due to pressures on component management to meet certain performance measures).
  - Controls over the group's financial reporting process.

#### *The Group's System of Internal Control*

##### The Nature and Extent of Commonality of Controls (Ref: Para. 30(c)(i))

- A93. Group management may design controls that are intended to operate in a common manner across multiple entities or business units (i.e., common controls). For example, group management may design common controls for inventory management, which operate using the same IT system and that are implemented across all entities or business units in the group. Common controls may exist in each component of the group's system of internal control, and they may be implemented at different levels within the group (e.g., at the level of the consolidated group as a whole, or for other levels of aggregation within the group). Common controls may be direct controls or indirect controls. Direct controls are controls that are precise enough to address risks of material misstatement at the assertion level. Indirect controls are controls that support direct controls.<sup>73</sup>
- A94. Understanding the components of the group's system of internal control includes understanding the commonality of the controls within those components across the group. In understanding the commonality of a control across the group, considerations that may be relevant include whether:
- The control is designed centrally and is required to be implemented as designed (i.e., without modification) at some or all components;
  - The control is implemented and, if applicable, monitored by individuals with similar responsibilities and capabilities at all the components where the control is implemented;
  - If a control uses information from IT applications, the IT applications and other aspects of the IT environment that generate the information are the same across the components or locations; or
  - If the control is automated, it is configured in the same way in each IT application across the components.

<sup>73</sup> ISA 315 (Revised 2019), paragraph A5

- A96. Judgment may often be needed to determine whether a control is a common control. For example, group management may require that all entities and business units perform a monthly evaluation of the aging of customers' accounts that are generated from a specific IT application. When the aging reports are generated from different IT applications or the implementation of the IT application differs across entities or business units, there may be a need to consider whether the control can be determined to be common. This is because of differences in the design of the control that may exist due to the existence of different IT applications (e.g., whether the IT application is configured in the same manner across components, and whether there are effective general IT controls across different IT applications).
- A97. Consideration of the level at which controls are performed within the group (e.g., at the level of the consolidated group as a whole or for other levels of aggregation within the group) and the degree of centralization and commonality may be important to the understanding of how information is processed and controlled. In some circumstances, controls may be performed centrally (e.g., performed only at a single entity or business unit), but may have a pervasive effect on other entities or business units (e.g., a shared service center that processes transactions on behalf of other entities or business units within the group). The processing of transactions and related controls at a shared service center may operate in the same way for those transactions being processed by the shared service center regardless of the entity or business unit (e.g., the processes, risks and controls may be the same regardless of the source of the transaction). In such cases, it may be appropriate to identify the controls and evaluate the design and determine the implementation of the controls, and, if applicable, test operating effectiveness, as a single population.

Centralized Activities (Ref: Para. 30(c)(i)–(ii))

- A98. Group management may centralize some of its activities, for example financial reporting or accounting functions may be performed for a particular group of common transactions or other financial information in a consistent and centralized manner for multiple entities or business units (e.g., when the initiation, authorization, recording, processing, or reporting of revenue transactions is performed at a shared service center).
- A99. Obtaining an understanding of how centralized activities fit into the overall group structure, and the nature of the activities undertaken, may help to identify and assess risks of material misstatement and appropriately respond to such risks. For example, controls at a shared service center may operate independently from other controls, or they may be dependent upon controls at an entity or business unit from which financial information is derived (e.g., sales transactions may be initiated and authorized at an entity or business unit, but the processing may occur at the shared service center).
- A100. The group auditor may involve component auditors in testing the operating effectiveness of common controls or controls related to centralized activities. In such circumstances, effective collaboration between the group auditor and component auditors is important as the audit evidence obtained through testing the operating effectiveness of common controls or controls related to centralized activities supports the determination of the nature, timing and extent of substantive procedures to be performed across the group.

Communications About Significant Matters that Support the Preparation of the Group Financial Statements (Ref: Para. 30(c)(iv))

- A101. Group entities or business units may use a financial reporting framework for statutory, regulatory or other reasons that is different from the financial reporting framework used for the group's

financial statements. In such circumstances, an understanding of group management’s financial reporting processes to align accounting policies and, when relevant, financial reporting periods that differ from that of the group, enables the group auditor to understand how adjustments, reconciliations and reclassifications are made, and whether they are made centrally by group management or by the entity or business unit.

#### Instructions by group management to entities or business units

A102. In applying ISA 315 (Revised 2019),<sup>74</sup> the group auditor is required to understand how group management communicates significant matters that support the preparation of the group financial statements. To achieve uniformity and comparability of financial information, group management may issue instructions (e.g., communicate financial reporting policies) to the entities or business units that include details about financial reporting processes or may have policies that are common across the group. Obtaining an understanding of group management’s instructions may affect the identification and assessment of the risks of material misstatement of the group financial statements. For example, inadequate instructions may increase the likelihood of misstatements due to the risk that transactions are incorrectly recorded or processed, or that accounting policies are incorrectly applied.

A103. The group auditor’s understanding of the instructions or policies may include the following:

- The clarity and practicality of the instructions for completing the reporting package.
- Whether the instructions:
  - Adequately describe the characteristics of the applicable financial reporting framework and the accounting policies to be applied;
  - Address information necessary to prepare disclosures that are sufficient to comply with the requirements of the applicable financial reporting framework, for example, disclosure of related party relationships and transactions, and segment information;
  - Address information necessary for making consolidation adjustments, for example, intra-group transactions and unrealized profits, and intra-group account balances; and
  - Include a reporting timetable.

#### *Considerations When Component Auditors Are Involved* (Ref: Para. 31–32)

A104. During the course of the group audit, the group auditor may communicate the matters in paragraph 31 to other component auditors, if these matters are relevant to the work of those component auditors. Paragraph A142 includes examples of other matters that may need to be communicated timely in the course of the component auditor’s work.

A105. The nature of related party relationships and transactions may, in some circumstances, give rise to higher risks of material misstatement of the financial statements than transactions with unrelated parties.<sup>75</sup> In a group audit there may be a higher risk of material misstatement of the group financial statements, including due to fraud, associated with related party relationships when:

- The group structure is complex;

<sup>74</sup> ISA 315 (Revised 2019), paragraph 25(b)

<sup>75</sup> ISA 550, paragraph 2

- The group's information systems are not integrated and therefore less effective in identifying and recording related party relationships and transactions; and
- There are numerous or frequent related party transactions between entities and business units.

Planning and performing the audit with professional skepticism, as required by ISA 200,<sup>76</sup> is therefore particularly important when these circumstances exist.

### **Identifying and Assessing the Risks of Material Misstatement** (Ref: Para. 33)

A106. The process to identify and assess the risks of material misstatement of the group financial statements is iterative and dynamic, and may be challenging, particularly when the component's activities are complex or specialized, or when there are many components across multiple locations. In applying ISA 315 (Revised 2019),<sup>77</sup> the auditor develops initial expectations about the potential risks of material misstatement and an initial identification of the significant classes of transactions, account balances and disclosures of the group financial statements based on their understanding of the group and its environment, the applicable financial reporting framework and the group's system of internal control.

A107. The initial expectations about the potential risks of material misstatement take into account the auditor's understanding of the group, including its entities or business units, and the environments and industries in which they operate. Based on the initial expectations, the group auditor may, and often will, involve component auditors in risk assessment procedures as they may have direct knowledge and experience with the entities or business units that may be helpful in understanding the activities and related risks, and where risks of material misstatement of the group financial statements may arise in relation to those entities or business units.

A108. For identified risks of material misstatement at the assertion level, the group auditor is required to take responsibility for assessing inherent risk. Such assessment involves assessing the likelihood and magnitude of misstatement, which takes into account how, and the degree to which:<sup>78</sup>

- Inherent risk factors affect the susceptibility of relevant assertions to misstatement.
- The risks of material misstatement at the group financial statement level affect the assessment of inherent risk for risks of material misstatement at the assertion level.

A109. Based on the risk assessment procedures performed, the group auditor may determine that an assessed risk of material misstatement of the group financial statements only arises in relation to financial information of certain components. For example, the risk of material misstatement relating to a legal claim may only exist in entities or business units that operate in a certain jurisdiction or in entities or business units that have similar operations or activities.

A110. Appendix 3 sets out examples of events and conditions that, individually or together, may indicate risks of material misstatement of the group financial statements, whether due to fraud or error, including with respect to the consolidation process.

### *Fraud*

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<sup>76</sup> ISA 200, paragraph 15

<sup>77</sup> ISA 315 (Revised 2019), paragraph A126

<sup>78</sup> ISA 315 (Revised 2019), paragraph 31

A111. In applying ISA 240,<sup>79</sup> the auditor is required to identify and assess the risks of material misstatement of the financial statements due to fraud, and to design and perform further audit procedures whose nature, timing and extent are responsive to the assessed risks of material misstatement due to fraud at the assertion level. Information used to identify the risks of material misstatement of the group financial statements due to fraud may include the following:

- Group management’s assessment of the risk that the group financial statements may be materially misstated due to fraud.
- Group management’s process for identifying and responding to the risks of fraud in the group financial statements, including any specific fraud risks identified by group management, or classes of transactions, account balances, or disclosures for which a risk of fraud is higher.
- Whether there are particular components which are more susceptible to risks of material misstatement due to fraud.
- Whether any fraud risk factors or indicators of management bias exist in the consolidation process.
- How those charged with governance of the group monitor group management’s processes for identifying and responding to the risks of fraud in the group, and the controls group management has established to mitigate these risks.
- Responses of those charged with governance of the group, group management, appropriate individuals within the internal audit function (and when appropriate, component management, the component auditors, and others) to the group auditor’s inquiry whether they have knowledge of any actual, suspected, or alleged fraud affecting a component or the group.

*Considerations When Component Auditors Are Involved (Ref: Para. 34)*

A112. When the group auditor involves component auditors in the design and performance of risk assessment procedures, the group auditor remains responsible for having an understanding of the group and its environment, the applicable financial reporting framework and the group’s system of internal control to have a sufficient basis for the identification and assessment of the risks of material misstatement of the group financial statements in accordance with paragraph 33.

A113. When the audit evidence obtained from the risk assessment procedures does not provide an appropriate basis for the identification and assessment of the risks of material misstatement, ISA 315 (Revised 2019)<sup>80</sup> requires the auditor to perform additional risk assessment procedures until audit evidence has been obtained to provide such a basis.

**Materiality**

*Component Performance Materiality (Ref: Para. 35(a))*

A114. Paragraph 35(a) requires the group auditor to determine component performance materiality for each of the components where audit procedures are performed on financial information that is disaggregated. The component performance materiality amount may be different for each component. Also, the component performance materiality amount for an individual component

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<sup>79</sup> ISA 240, paragraphs 26, 31

<sup>80</sup> ISA 315 (Revised 2019), paragraph 35

need not be an arithmetical portion of the group performance materiality and, consequently, the aggregate of component performance materiality amounts may exceed group performance materiality.

A115. This ISA does not require component performance materiality to be determined for each class of transactions, account balance or disclosure for components at which audit procedures are performed. However, if, in the specific circumstances of the group, there is one or more particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the group financial statements as a whole could reasonably be expected to influence the economic decisions of users taken on the basis of the group financial statements, ISA 320<sup>81</sup> requires a determination of the materiality level or levels to be applied to those particular classes of transactions, account balances or disclosures. In these circumstances, the group auditor may need to consider whether a component performance materiality lower than the amount communicated to the component auditor may be appropriate for those particular classes of transactions, account balances or disclosures.<sup>82</sup>

A116. The determination of component performance materiality is not a simple mechanical calculation and involves the exercise of professional judgment. Factors the group auditor may take into account in setting component performance materiality include the following:

- The extent of disaggregation of the financial information across components (e.g., as the extent of disaggregation across components increases, a lower component performance materiality ordinarily would be appropriate to address aggregation risk). The relative significance of the component to the group may affect the extent of disaggregation (e.g., if a single component represents a large portion of the group, there likely may be less disaggregation across components).
- Expectations about the nature, frequency, and magnitude of misstatements in the component financial information, for example:
  - Whether there are risks that are unique to the financial information of the component (e.g., industry-specific accounting matters, unusual or complex transactions).
  - The nature and extent of misstatements identified at the component in prior audits.

A117. To address aggregation risk, paragraph 35(a) requires component performance materiality to be lower than group performance materiality. As explained in paragraph A116, as the extent of disaggregation across components increases, a lower component performance materiality amount ordinarily would be appropriate to address aggregation risk. In some circumstances, however, component performance materiality may be set at an amount closer to group performance materiality because there is less aggregation risk, such as when the financial information for one component represents a substantial portion of the group financial statements. When determining component performance materiality for a non-controlling interest in an entity that is accounted for by the equity method, the group auditor may take into account the group's ownership percentage and the share of the investee's profits and losses.

A118. In some cases, further audit procedures may be performed by the group auditor or a component auditor on a significant class of transactions or significant account balance as a single population (i.e., not disaggregated across components). In such cases, group performance materiality often will be used for purposes of performing these procedures.

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<sup>81</sup> ISA 320, paragraphs 10 and A11–A12

<sup>82</sup> ISA 320, paragraph A13

*'Clearly Trivial' Threshold (Ref: Para: 35(b))*

A119. The threshold for communicating misstatements to the group auditor is set at an amount equal to, or lower than, the amount regarded as clearly trivial for the group financial statements. In accordance with ISA 450,<sup>83</sup> this threshold is the amount below which misstatements would not need to be accumulated because the group auditor expects that the accumulation of such amounts clearly would not have a material effect on the group financial statements.

*Considerations When Component Auditors Are Involved*

Communicating Component Performance Materiality (Ref: Para. 36)

A120. In some cases, it may be appropriate for the group auditor to involve the component auditor in determining an appropriate component performance materiality amount, in view of the component auditor's knowledge of the component and potential sources of misstatement of the component financial information. In this regard, the group auditor also may consider communicating group performance materiality to the component auditor to support collaboration in determining whether component performance materiality, in relation to group performance materiality, is appropriate in the circumstances.

A121. Component performance materiality is based, at least in part, on expectations about the nature, frequency, and magnitude of misstatements in the component financial information. Therefore, ongoing communication between the component auditor and the group auditor is important, particularly if the number and magnitude of misstatements identified by the component auditor are higher than expected.

**Responding to the Assessed Risks of Material Misstatement (Ref: Para. 37)**

*Performing Further Audit Procedures*

Performing Further Audit Procedures Centrally

A122. Further audit procedures may be designed and performed centrally if the audit evidence to be obtained from performing further audit procedures on one or more significant classes of transactions, account balances or disclosures in the aggregate will respond to the assessed risks of material misstatement, for example, if the accounting records for the revenue transactions of the entire group are maintained centrally (e.g., at a shared service center). Factors that may be relevant to the auditor's determination of whether to perform further audit procedures centrally include, for example:

- The level of centralization of activities relevant to financial reporting.
- The nature and extent of commonality of controls.
- The similarity of the group's activities and business lines.

A123. The group auditor may determine that the financial information of several components can be considered as one population for the purpose of performing further audit procedures, for example, when transactions are considered to be homogenous because they share the same characteristics, the related risks of material misstatement are the same, and controls are designed and operating in a consistent way.

A124. When further audit procedures are performed centrally, component auditors may still be involved. For example, when the group has multiple shared service centers, the group auditor may involve

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<sup>83</sup> ISA 450, paragraph A3

component auditors in the performance of further audit procedures for these shared service centers.

#### Performing Further Audit Procedures at the Component Level

A125. In other circumstances, procedures to respond to the risks of material misstatement of the group financial statements that are related to the financial information of a component may be more effectively performed at the component level. This may be the case when the group has:

- Different revenue streams;
- Multiple lines of business;
- Operations across multiple locations; or
- Decentralized systems of internal control.

#### Large Number of Components Whose Financial Information Is Individually Immaterial but Material in the Aggregate to the Group Financial Statements

A126. A group may be comprised of a large number of components whose financial information is individually immaterial but material in the aggregate to the group financial statements. Circumstances such as these in which the significant classes of transactions, account balances or disclosures in the group financial statements are disaggregated over a large number of components may present additional challenges for the group auditor in planning and performing further audit procedures.

A127. In some cases, it may be possible to obtain sufficient appropriate audit evidence by performing further audit procedures centrally on these significant classes of transactions, account balances or disclosures (e.g., if they are homogeneous, subject to common controls and access to appropriate information can be obtained). The further audit procedures may also include substantive analytical procedures in accordance with ISA 520.<sup>84</sup> Depending on the circumstances of the engagement, the financial information of the components may be aggregated at appropriate levels for purposes of developing expectations and determining the amount of any difference of recorded amounts from expected values in performing the substantive analytical procedures. The use of automated tools and techniques may be helpful in these circumstances.

A128. In other cases, it may be necessary to perform further audit procedures at selected components to address the risks of material misstatement of the group financial statements. The determination of the components at which audit procedures are to be performed, and the nature, timing and extent of further audit procedures to be performed at the selected components, are matters of professional judgment. In these circumstances, introducing an element of unpredictability in the components selected for testing also may be helpful in relation to the risks of material misstatement of the group financial statements due to fraud (also see paragraph A134).

#### *The Nature and Extent of Further Audit Procedures*

A129. In response to the assessed risks of material misstatement, the group auditor may determine the following scope of work to be appropriate at a component (with the involvement of component auditors, as applicable):

- Design and perform further audit procedures on the entire financial information of the component;

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<sup>84</sup> ISA 520, *Analytical Procedures*

- Design and perform further audit procedures on one or more classes of transactions, account balances or disclosures; or
- Perform specific further audit procedures.

A130. Although the group auditor takes responsibility for the nature, timing and extent of further audit procedures to be performed, component auditors can be, and often are, involved in all phases of the group audit, including in the design and performance of further audit procedures.

#### Design and Perform Further Audit Procedures on the Entire Financial Information of the Component

A131. The group auditor may determine that designing and performing further audit procedures on the entire financial information of a component is an appropriate approach, including when:

- Audit evidence needs to be obtained on all or a significant proportion of a component's financial information to respond to the assessed risks of material misstatement of the group financial statements.
- There is a pervasive risk of material misstatement of the group financial statements due to the existence of events or conditions at the component that may be relevant to the group auditor's evaluation of group management's assessment of the group's ability to continue as a going concern.

Design and perform further audit procedures on one or more classes of transactions, account balances or disclosures

A132. The group auditor may determine that designing and performing further audit procedures on one or more particular classes of transactions, account balances, or disclosures of the financial information of a component is an appropriate approach to address assessed risks of material misstatement of the group financial statements. For example, a component may have limited operations but holds a significant portion of the land and buildings of the group or has significant tax balances.

Perform specific further audit procedures

A133. The group auditor may determine that designing and performing specific further audit procedures on the financial information of a component is an appropriate approach, such as when audit evidence needs to be obtained for one or more relevant assertions only. For example, the group auditor may centrally test the class of transaction, account balance or disclosure and may require the component auditor to perform specific further audit procedures at the component (e.g., specific further audit procedures related to the valuation of claims or litigations in the component's jurisdiction or the existence of an asset).

#### *Element of Unpredictability*

A134. Incorporating an element of unpredictability in the type of work to be performed, the entities or business units at which procedures are performed and the extent to which the group auditor is involved in the work, may increase the likelihood of identifying a material misstatement of the components' financial information that may give rise to a material misstatement of the group financial statements due to fraud.<sup>85</sup>

#### *Operating Effectiveness of Controls*

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<sup>85</sup> ISA 240, paragraph 30(c)

A135. The group auditor may rely on the operating effectiveness of controls that operate throughout the group in determining the nature, timing and extent of substantive procedures to be performed at either the group level or at the components. ISA 330<sup>86</sup> requires the auditor to design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of those controls. Component auditors may be involved in designing and performing such tests of controls.

A136. If deviations from controls upon which the auditor intends to rely are detected, ISA 330<sup>87</sup> requires the auditor to make specific inquiries to understand these matters and their potential consequences. If more deviations than expected are detected as a result of testing the operating effectiveness of the controls, the group auditor may need to revise the group audit plan. Possible revisions to the group audit plan may include:

- Requesting additional substantive procedures to be performed at certain components.
- Identifying and testing the operating effectiveness of other relevant controls that are designed and implemented effectively.
- Increasing the number of components selected for further audit procedures.

A137. When the operating effectiveness of controls is tested centrally (e.g., controls at a shared service center or testing of common controls), the group auditor may need to communicate information about the audit work performed to the component auditors. For example, when a component auditor is requested to design and perform substantive procedures on the entire financial information of the component, or design and perform substantive procedures on one or more classes of transactions, account balances or disclosures, the component auditor may discuss with the group auditor about the control testing performed centrally to determine the nature, timing and extent of the substantive procedures.

#### *Consolidation Process*

##### Consolidation Procedures (Ref: Para. 38(a))

A138. The further audit procedures on the consolidation, including sub-consolidations, may include:

- Determining that the necessary journal entries are reflected in the consolidation; and
- Evaluating the operating effectiveness of the controls over the consolidation process and responding appropriately if any controls are determined to be ineffective.

##### Consolidation Adjustments and Reclassifications (Ref: Para. 38(c))

A139. The consolidation process may require adjustments and reclassifications to amounts reported in the group financial statements that do not pass through the usual IT applications, and may not be subject to the same controls to which other financial information is subject. The group auditor's evaluation of the appropriateness, completeness and accuracy of the adjustments and reclassifications may include:

- Evaluating whether significant adjustments appropriately reflect the events and transactions underlying them;
- Determining whether those entities or business units whose financial information has been included in the group financial statements were appropriately included;

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<sup>86</sup> ISA 330, paragraph 8

<sup>87</sup> ISA 330, paragraph 17

- Determining whether significant adjustments have been correctly calculated, processed and authorized by group management and, when applicable, by component management;
- Determining whether significant adjustments are properly supported and sufficiently documented; and
- Evaluating the reconciliation and elimination of intra-group transactions, unrealized profits, and intra-group account balances.

*Considerations When Component Auditors Are Involved (Ref: Para. 42–43)*

A140. When the group auditor involves component auditors in the design or performance of further audit procedures, the component auditor may determine that the use of the work of an auditor's expert is appropriate and communicate this to the group auditor. In such circumstances, when determining whether the component auditor's design and performance of further audit procedures is appropriate, the group auditor may, for example, discuss with the component auditor:

- The nature, scope and objectives of the auditor's expert's work.
- The component auditor's evaluation of the adequacy of the work of the auditor's expert for the group auditor's purposes.

A141. The appropriate level of the group auditor's involvement may depend on the circumstances and the structure of the group and other factors, such as the group auditor's previous experience with the component auditors that perform procedures on the consolidation and sub-consolidations and the circumstances of the group audit engagement (e.g., if the financial information of an entity or business unit has not been prepared in accordance with the same accounting policies applied to the group financial statements).

**Evaluating the Component Auditor's Communication and the Adequacy of Their Work**

*Communication about Matters Relevant to the Group Auditor's Conclusion with Regard to the Group Audit (Ref: Para. 45)*

A142. Although the matters required to be communicated in accordance with paragraph 45 are relevant to the group auditor's conclusion with regard to the group audit, certain matters may be communicated during the course of the component auditor's procedures. In addition to the matters in paragraphs 32 and 50, such matters may include, for example:

- Information about breaches of relevant ethical requirements, including identified breaches of independence provisions;
- Information about instances of non-compliance with laws or regulations;
- Newly arising significant risks of material misstatement, including risks of fraud;
- Identified or suspected fraud or illegal acts involving component management or employees that could have a material effect on the group financial statements; or
- Significant and unusual transactions.

*Communication of Misstatements of Component Financial Information (Ref: Para. 45(e))*

A143. Knowledge about corrected and uncorrected misstatements across components may alert the group auditor to potential pervasive internal control deficiencies, when considered along with the communication of deficiencies in accordance with paragraph 45(g). In addition, a higher than expected number of identified misstatements (uncorrected or corrected) may indicate a higher

risk of undetected misstatements, which may lead the group auditor to conclude that additional audit procedures need to be performed at certain components.

*Component Auditor's Overall Findings or Conclusions* (Ref: Para. 45(k))

A144. The form and content of the deliverables from the component auditor are influenced by the nature and extent of the audit work the component auditor has been requested to perform. The group auditor's firm policies or procedures may address the form or specific wording of an overall conclusion from the component auditor on the audit work performed for purposes of the group audit. In some cases, local law or regulation may specify the form of conclusion (e.g., an opinion) to be provided by the component auditor.

*Evaluating Whether Communications with the Component Auditor Are Adequate for the Group Auditor's Purposes* (Ref: Para. 46(b))

A144A. If the group auditor determines that the component auditor's communications are not adequate for the group auditor's purposes, the group auditor may consider whether, for example:

- Further information can be obtained from the component auditor (e.g., through further discussions or meetings);
- It is necessary to review additional component auditor audit documentation in accordance with paragraph 47;
- Additional audit procedures may need to be performed in accordance with paragraph 48; or
- There are any concerns about the component auditor's competence or capabilities.

*Reviewing Additional Component Auditor Audit Documentation* (Ref: Para. 47)

A145. Paragraph A72 provides guidance for the group auditor in tailoring the nature, timing and extent of the direction and supervision of the component auditor, and the review of their work, based on the facts and circumstances of the group audit and other matters (e.g., the assessed risks of material misstatement of the group financial statements). The group auditor's consideration in accordance with paragraph 47(c) also may be affected by the following matters relevant to the group auditor's ongoing involvement in the work of the component auditor:

- Communications from the component auditor, including those in accordance with paragraph 45 of this ISA; and
- The review of component auditor audit documentation by the group auditor during the course of the group audit (e.g., to fulfill the requirements of paragraphs 34, 42 and 43) or by the group engagement partner in accordance with paragraph 31 of ISA 220 (Revised).

A146. Other factors that may affect the group auditor's determination about whether, and the extent to which, it is necessary to review additional component auditor audit documentation in the circumstances include:

- The degree to which the component auditor was involved in risk assessment procedures and in the identification and assessment of the risks of material misstatement of the group financial statements;
- The significant judgments made by, and the findings or conclusions of, the component auditor about matters that are material to the group financial statements;
- The competence and capabilities of more experienced engagement team members from

the component auditor responsible for reviewing the work of less experienced individuals; and

- Whether the component auditor and group auditor are subject to common policies or procedures for review of audit documentation.

### **Subsequent Events** (Ref: Para. 49–50)

A147. The group auditor may:

- Request a component auditor to perform subsequent events procedures to assist the group auditor to identify events that occur between the dates of the financial information of the components and the date of the auditor’s report on the group financial statements.
- Perform procedures to cover the period between the date of communication of subsequent events by the component auditor and the date of the auditor’s report on the group financial statements.

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

*Sufficiency and Appropriateness of Audit Evidence* (Ref: Para. 51)

A148. The audit of group financial statements is a cumulative and iterative process. As the group auditor performs planned audit procedures, the audit evidence obtained may cause the group auditor to modify the nature, timing or extent of other planned audit procedures as information may come to the group auditor’s attention that differs significantly from the information on which the risk assessment was based. For example:

- The misstatements identified at a component may need to be considered in relation to other components; or
- The group auditor may become aware of access restrictions to information or people at a component because of changes in the environment (e.g., war, civil unrest or outbreaks of disease).

In such circumstances, the group auditor may need to reevaluate the planned audit procedures, based on the revised consideration of assessed risks for all or some of the significant classes of transactions, account balances, or disclosures and related assertions.

A149. The evaluation required by paragraph 51 assists the group auditor in determining whether the overall group audit strategy and group audit plan developed to respond to the assessed risks of material misstatement of the group financial statements continues to be appropriate. The requirement in ISA 330<sup>88</sup> for the auditor, irrespective of the assessed risks of material misstatement, to design and perform substantive procedures for each material class of transactions, account balance, and disclosure also may be helpful for purposes of this evaluation in the context of the group financial statements.

A150. The group auditor may consider the engagement team’s exercise of professional skepticism when evaluating the sufficiency and appropriateness of audit evidence obtained. For example, the group auditor may consider whether matters such as those described in paragraph A16 have inappropriately led the engagement team to:

- Obtain audit evidence that is easier to access without giving appropriate consideration to its relevance and reliability:

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<sup>88</sup> ISA 330, paragraph 18

- Obtain less persuasive evidence than is necessary in the circumstances; or
- Design and perform audit procedures in a manner that is biased towards obtaining evidence that is corroborative or excluding evidence that is contradictory.

A151. ISA 220 (Revised)<sup>89</sup> requires the engagement partner to determine, on or before the date of the auditor's report, through review of audit documentation and discussion with the engagement team, that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor's report to be issued. Information that may be relevant to the group auditor's evaluation of the audit evidence obtained from the work performed by component auditors depends on the facts and circumstances of the group audit, and may include:

- The communications from the component auditors required by paragraph 45, including the overall findings or conclusions of the component auditors on the work performed for purposes of the group audit;
- Other communications from the component auditors throughout the group audit, including those required by paragraph 32; and
- The group auditor's direction and supervision of the component auditors, and review of their work, including, as applicable, the group auditor's review of additional component auditor audit documentation in accordance with paragraph 47.

A152. In some circumstances, an overall summary memorandum describing the work performed and the results thereof may provide a basis on its own for the group auditor to conclude that the work performed and audit evidence obtained by the component auditor is sufficient for purposes of the group audit. This may be the case, for example, when the component auditor has been requested to perform specific further audit procedures as identified and communicated by the group auditor.

*Evaluating the Effect on the Group Audit Opinion (Ref: Para. 52)*

A153. The group engagement partner's evaluation may include a consideration of whether corrected and uncorrected misstatements communicated by component auditors indicate a systemic issue (e.g., regarding transactions subject to common accounting policies or common controls) that may affect other components.

**Auditor's Report (Ref: Para. 53)**

A154. Although component auditors may perform work on the financial information of the components for the group audit and as such are responsible for their overall findings or conclusions, the group engagement partner or the group engagement partner's firm is responsible for the group audit opinion.

A155. When the group audit opinion is modified because the group auditor was unable to obtain sufficient appropriate audit evidence in relation to the financial information of one or more components, the Basis for Qualified Opinion or Basis for Disclaimer of Opinion section in the auditor's report on the group financial statements describes the reasons for that inability.<sup>90</sup> In some circumstances, a reference to a component auditor may be necessary to adequately describe the reasons for the modified opinion, for example, when the component auditor is unable to perform or complete the work requested on the component financial information due to circumstances beyond the control of component management.

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<sup>89</sup> ISA 220 (Revised), paragraph 32

<sup>90</sup> ISA 705 (Revised), paragraphs 20 and 24

**Communication with Group Management and Those Charged with Governance of the Group***Communication with Group Management* (Ref: Para. 54–56)

A156. The group audit may be complex due to the number and nature of the entities and business units comprising the group. In addition, as explained in paragraph A7, the group auditor may determine that certain entities or business units may be considered together as a component for purposes of planning and performing the group audit. Therefore, discussing with group management an overview of the planned scope and timing may help in coordinating the work performed at components, including when component auditors are involved, and in identifying component management (see paragraph A22).

A157. ISA 240<sup>91</sup> contains requirements and guidance on the communication of fraud to management and, when management may be involved in the fraud, to those charged with governance.

A158. Group management may need to keep certain material sensitive information confidential. Examples of matters that may be significant to the financial statements of the component of which component management may be unaware include the following:

- Potential litigation.
- Plans for abandonment of material operating assets.
- Subsequent events.
- Significant legal agreements.

A159. Group management may inform the group auditor about non-compliance or suspected non-compliance with laws or regulations in entities or business units within the group. Paragraph A84 provides guidance for the group engagement partner in these circumstances.

*Communication with Those Charged with Governance of the Group* (Ref: Para. 57)

A160. The matters the group auditor communicates to those charged with governance of the group may include those brought to the attention of the group auditor by component auditors that the group auditor judges to be significant to the responsibilities of those charged with governance of the group. Communication with those charged with governance of the group may take place at various times during the group audit. For example, the matter referred to in paragraph 57(a) may be communicated after the group auditor has determined the work to be performed on the financial information of the components. On the other hand, the matter referred to in paragraph 57(b) may be communicated at the end of the audit, and the matters referred to in paragraph 57(c)–(d) may be communicated when they occur.

A161. ISA 260 (Revised)<sup>92</sup> requires the auditor to communicate with those charged with governance an overview of the planned scope and timing of the audit. For a group audit, this communication helps those charged with governance understand the group auditor's determination of the components at which audit work will be performed, including whether certain of the group's entities or business units will be considered together as a component, and the planned involvement of component auditors. This communication also helps to enable a mutual understanding of and discussion about the group and its environment (see paragraph 30) and areas, if any, in which those charged with governance may request the group auditor to undertake additional procedures.

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<sup>91</sup> ISA 240, paragraphs 41–43

<sup>92</sup> ISA 260 (Revised), paragraph 15

*Communication of Identified Deficiencies in Internal Control (Ref: Para. 58)*

A162. The group auditor is responsible for determining, on the basis of the audit work performed, whether one or more identified deficiencies, individually or in combination, constitute significant deficiencies.<sup>93</sup> The group auditor may request input from the component auditor about whether an identified deficiency or combination of deficiencies at the component is a significant deficiency in internal control.

**Documentation (Ref: Para. 59)**

A163. Other ISAs contain specific documentation requirements that are intended to clarify the application of ISA 230 in the particular circumstances of those other ISAs. The Appendix to ISA 230 lists other ISAs that contain specific documentation requirements and guidance.

A164. The audit documentation for the group audit supports the group auditor's evaluation in accordance with paragraph 51 as to whether sufficient appropriate audit evidence has been obtained on which to base the group audit opinion. Also see paragraph A151.

A165. The audit documentation for the group audit comprises:

- The documentation in the group auditor's file; and
- The separate documentation in the respective component auditor files relating to the work performed by the component auditors for purposes of the group audit (i.e., component auditor audit documentation).

A166. The final assembly and retention of the audit documentation for a group audit is subject to the policies or procedures of the group auditor's firm in accordance with ISQM 1.<sup>94</sup> The group auditor may provide specific instructions to component auditors regarding the assembly and retention of the documentation of work performed by them for purposes of the group audit.

*Basis for the Group Auditor's Determination of Components (Ref: Para: 59(b))*

A167. The basis for the group auditor's determination of components may be documented in various ways, including, for example, documentation related to the fulfillment of the requirements in paragraphs 22, 33 and 57(a) of this ISA.

*Basis for the Group Auditor's Determination of the Competence and Capabilities of Component Auditors (Ref: Para: 59(d))*

A168. ISQM 1<sup>95</sup> provides guidance on matters that the firm's policies or procedures may address regarding the competence and capabilities of the engagement team members. Such policies or procedures may describe or provide guidance about how to document the determination of the competence and capabilities of the engagement team, including component auditors. For example, the confirmation obtained from the component auditor in accordance with paragraph 24 may include information about the component auditor's relevant industry experience. The group auditor also may ask for confirmation that the component auditor has sufficient time to perform the assigned audit procedures (see paragraph A59).

*Documentation of the Direction and Supervision of Component Auditors and the Review of Their*

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<sup>93</sup> ISA 265, paragraph 8

<sup>94</sup> ISQM 1, paragraphs 31(f) and A83–A85

<sup>95</sup> ISQM 1, paragraph A96

*Work* (Ref: Para. 59(f))

A169. As described in paragraph A72, the approach to direction, supervision and review in a group audit will be tailored by the group auditor based on the facts and circumstances of the engagement, and will generally include a combination of addressing the group auditor's firm policies or procedures and responses specific to the group audit. Such policies or procedures may also describe or provide guidance about the documentation of the group auditor's direction and supervision of the engagement team and the review of their work.

A170. ISA 300<sup>96</sup> requires the auditor to develop an audit plan that includes a description of the nature, timing and extent of the planned direction and supervision of engagement team members and the review of their work. When component auditors are involved, the extent of such descriptions will often vary by component, recognizing that the planned nature, timing and extent of direction and supervision of component auditors, and review of their work, may be influenced by the matters described in paragraph A48.

A171. The group auditor's documentation of the direction and supervision of component auditors and the review of their work may include, for example:

- Required communications with component auditors, including instructions issued and other confirmations required by this ISA.
- The rationale for the selection of visits to component auditor sites, attendees at meetings and the nature of the matters discussed.
- Matters discussed in meetings with component auditors or component management.
- The rationale for the group auditor's determination of component auditor audit documentation selected for review.
- Changes in the planned nature and extent of involvement in the work of component auditors, and the reasons why (e.g., assigning more experienced engagement team members in areas of the audit that are more complex or subjective than initially anticipated).

A172. Paragraph 47 requires the group auditor to determine whether, and the extent to which it is necessary to review additional component auditor audit documentation. Paragraphs A145–A146 provide guidance for the group auditor in making this determination.

A173. Component auditor audit documentation ordinarily need not be replicated in the group auditor's audit file. However, the group auditor may decide to summarize, replicate or retain copies of certain component auditor documentation in the group auditor's audit file to supplement the description of a particular matter in communications from the component auditor, including the matters required to be communicated by this ISA. Examples of such component auditor documentation may include:

- A listing or summary of the significant judgments made by the component auditor, and the conclusions reached thereon, that are relevant to the group audit;
- Matters that may need to be communicated to those charged with governance of the group; or
- Matters that may be determined to be key audit matters to be communicated in the auditor's report on the group financial statements.

A174. When required by law or regulation, certain component auditor documentation may need to be

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<sup>96</sup> ISA 300, paragraph 9

included in the group auditor's audit file, for example, to respond to the request of a regulatory authority to review documentation related to work performed by a component auditor.

A175. Policies or procedures established by the firm in accordance with the firm's system of quality management, or resources provided by the firm or a network, may assist the group auditor in documenting the direction and supervision of component auditors and the review of their work. For example, an electronic audit tool may be used to facilitate communications between the group auditor and component auditors. The electronic audit tool also may be used for audit documentation, including providing information about the reviewer(s) and the date(s) and extent of their review.

*Additional Considerations When Access to Component Auditor Audit Documentation is Restricted*

(Ref: Para. 59)

A176. Audit documentation for a group audit may present some additional complexities or challenges in certain circumstances. This may be the case, for example, when law or regulation restrict the component auditor from providing documentation outside of its jurisdiction, or when war, civil unrest or outbreaks of disease restrict access to relevant component auditor audit documentation.

A177. The group auditor may be able to overcome such restrictions by, for example:

- Visiting the location of the component auditor, or meeting with the component auditor in a location different from where the component auditor is located, to review the component auditor's audit documentation;
- Reviewing the relevant audit documentation remotely through the use of technology, when not prohibited by law or regulation;
- Requesting the component auditor to prepare and provide a memorandum that addresses the relevant information and holding discussions with the component auditor, if necessary, to discuss the contents of the memorandum; or
- Discussing with the component auditor the procedures performed, the evidence obtained and the conclusions reached by the component auditor.

It is a matter of professional judgment whether one or more of the actions described above may be sufficient to overcome the restrictions depending on the facts and circumstances of the group audit.

A178. When access to component auditor audit documentation is restricted, the group auditor's documentation nonetheless needs to comply with the requirements of the ISAs, including those relating to the documentation of the nature, timing and extent of the group auditor's direction and supervision of component auditors and the review of their work. The guidance in paragraphs A145–A146 may be helpful in determining the extent of the group auditor's review of the component auditor audit documentation in these circumstances. Paragraphs A173 and A174 provide examples of circumstances in which certain component auditor audit documentation may be included in the group auditor's audit file.

A179. If the group auditor is unable to overcome restrictions on access to the component auditor audit documentation, the group auditor may need to consider whether a scope limitation exists that may require a modification to the opinion on the group financial statements. See paragraph A42.

## Appendix 1

(Ref: Para. A42)

### Illustration of Independent Auditor’s Report When the Group Auditor Is Not Able to Obtain Sufficient Appropriate Audit Evidence on Which to Base the Group Audit Opinion

For purposes of this illustrative auditor’s report, the following circumstances are assumed:

- **Audit of a complete set of consolidated financial statements of an entity other than a listed entity using a fair presentation framework. The audit is a group audit of an entity with subsidiaries (i.e., ISA 600 (Revised) applies).**
- **The consolidated financial statements are prepared by management of the entity in accordance with IFRSs (a general purpose framework).**
- **The terms of the audit engagement reflect the description of management’s responsibility for the consolidated financial statements in ISA 210.**
- **The group auditor is unable to obtain sufficient appropriate audit evidence relating to a component accounted for by the equity method (recognized at \$15 million in the statement of financial position, which reflects total assets of \$60 million) because the group auditor did not have access to the accounting records, management, or auditor of the component.**
- **The group auditor has read the audited financial statements of the component as at December 31, 20X1, including the auditor’s report thereon, and considered related financial information kept by group management in relation to the component.**
- **In the group engagement partner’s judgment, the effect on the group financial statements of this inability to obtain sufficient appropriate audit evidence is material but not pervasive.<sup>1</sup>**
- **The IESBA Code comprises all of the relevant ethical requirements that apply to the audit.**
- **Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern in accordance with ISA 570 (Revised).**
- **The auditor is not required, and has otherwise not decided, to communicate key audit matters in accordance with ISA 701.<sup>2</sup>**
- **The auditor has obtained all of the other information prior to the date of the auditor’s report and the qualified opinion on the consolidated financial statements also affects the other information.**
- **Those responsible for oversight of the consolidated financial statements differ from those responsible for the preparation of the consolidated financial statements.**
- **In addition to the audit of the consolidated financial statements, the auditor has other reporting responsibilities required under local law.**

<sup>1</sup> If, in the group engagement partner’s judgment, the effect on the group financial statements of the inability to obtain sufficient appropriate audit evidence is material and pervasive, the group engagement partner would disclaim an opinion in accordance with ISA 705 (Revised).

<sup>2</sup> ISA 701, *Communicating Key Audit Matters in the Independent Auditor’s Report*

## INDEPENDENT AUDITOR’S REPORT

To the Shareholders of ABC Company [or Other Appropriate Addressee]

### Report on the Audit of the Consolidated Financial Statements<sup>3</sup>

#### Qualified Opinion

We have audited the consolidated financial statements of ABC Company and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 20X1, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion section of our report, the accompanying consolidated financial statements present fairly, in all material respects (or give a true and fair view of), the consolidated financial position of the Group as at December 31, 20X1, and (of) its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

#### Basis for Qualified Opinion

ABC Company’s investment in XYZ Company, a foreign associate acquired during the year and accounted for by the equity method, is carried at \$15 million on the consolidated statement of financial position as at December 31, 20X1, and ABC’s share of XYZ’s net income of \$1 million is included in the consolidated statement of comprehensive income for the year then ended. We were unable to obtain sufficient appropriate audit evidence about the carrying amount of ABC’s investment in XYZ as at December 31, 20X1 and ABC’s share of XYZ’s net income for the year because we were denied access to the financial information, management, and the auditors of XYZ. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants’ *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

#### Other Information [or another title if appropriate such as “Information Other than the Financial Statements and Auditor’s Report Thereon”]

[Reporting in accordance with the reporting requirements in ISA 720 (Revised)<sup>4</sup> – see Illustration 6 in Appendix 2 of ISA 720 (Revised). The last paragraph of the other information section in Illustration 6 would be customized to describe the specific matter giving rise to the qualified opinion that also affects the other information.]

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<sup>3</sup> The sub-title, “Report on the Audit of the Consolidated Financial Statements” is unnecessary in circumstances when the second sub-title, “Report on Other Legal and Regulatory Requirements” is not applicable.

<sup>4</sup> ISA 720 (Revised), *The Auditor’s Responsibilities Relating to Other Information*

**Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements<sup>5</sup>**

*[Reporting in accordance with ISA 700 (Revised)<sup>6</sup> – see Illustration 2 in ISA 700 (Revised).]*

**Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements**

*[Reporting in accordance with ISA 700 (Revised) – see Illustration 2 in ISA 700 (Revised). The last two paragraphs which are applicable for audits of listed entities only would not be included.]*

**Report on Other Legal and Regulatory Requirements**

*[Reporting in accordance with ISA 700 (Revised) – see Illustration 2 in ISA 700 (Revised).]*

*[Signature in the name of the audit firm, the personal name of the auditor, or both, as appropriate for the particular jurisdiction]*

*[Auditor Address]*

*[Date]*

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<sup>5</sup> Throughout these illustrative auditor’s reports, the terms management and those charged with governance may need to be replaced by another term that is appropriate in the context of the legal framework in the particular jurisdiction.

<sup>6</sup> ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

## Appendix 2

(Ref: Para. A85)

### Understanding the Group's System of Internal Control

1. This appendix provides examples of matters related to internal control that may be helpful in obtaining an understanding of the system of internal control in the context of a group environment, and expands on how ISA 315 (Revised 2019)<sup>1</sup> is to be applied in relation to an audit of group financial statements. The examples may not be relevant to every group audit engagement and the list of examples is not necessarily complete.

#### Control Environment

2. The group auditor's understanding of the control environment may include matters such as the following:
  - The structure of the governance and management functions across the group, and group management's oversight responsibilities, including arrangements for assigning authority and responsibility to management of entities or business units in the group.
  - How oversight over the group's system of internal control by those charged with governance is structured and organized.
  - How ethical and behavioral standards are communicated and reinforced in practice across the group, (e.g., group-wide programs, such as codes of conduct and fraud prevention programs).
  - The consistency of policies and procedures across the group, including a group financial reporting procedures manual.

#### The Group's Risk Assessment Process

3. The group auditor's understanding of the group's risk assessment process may include matters such as group management's risk assessment process, that is, the process for identifying, analyzing and managing business risks, including the risk of fraud, that may result in material misstatement of the group financial statements. It may also include an understanding of how sophisticated the group's risk assessment process is and the involvement of entities and business units in this process.

#### The Group's Process to Monitor the System of Internal Control

4. The group auditor's understanding of the group's process to monitor the system of internal control may include matters such as monitoring of controls, including how the controls are monitored across the group and, when relevant, activities of the internal audit function across the group. The group's internal audit function, including its nature, responsibilities and activities in respect of monitoring of controls at entities or business units in the group. ISA 610 (Revised 2013)<sup>2</sup> requires the auditor to evaluate the extent to which the internal audit function's organizational status and relevant policies and procedures support the objectivity of internal auditors, the level of competence of the internal audit function, and whether the internal audit function applies a systematic and disciplined approach, including quality control.

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<sup>1</sup> ISA 315 (Revised 2019), Appendix 3

<sup>2</sup> ISA 610 (Revised 2013), *Using the Work of Internal Auditors*, paragraph 15

## The Information System and Communication

5. The group auditor's understanding of the group's information system and communication may include matters such as the following:
- The extent of centralization in the group's IT environment and the commonality of IT applications, IT processes and IT infrastructure.
  - Group management's monitoring of operations and the financial results of entities or business units in the group, including regular reporting routines, which enables group management to monitor performance against budgets, and to take appropriate action.
  - Monitoring, controlling, reconciling, and eliminating intra-group transactions and unrealized profits, and intra-group account balances at group level.
  - A process for monitoring the timeliness and evaluating the accuracy and completeness of financial information received from entities or business units in the group.

### *Consolidation Process*

6. The group auditor's understanding of the consolidation process may include matters such as the following:
- Matters relating to the applicable financial reporting framework:
  - The extent to which management of entities or business units in the group have an understanding of the applicable financial reporting framework.
  - The process for identifying and accounting for entities or business units in the group in accordance with the applicable financial reporting framework.
  - The process for identifying reportable segments for segment reporting in accordance with the applicable financial reporting framework.
  - The process for identifying related party relationships and related party transactions for reporting in accordance with the applicable financial reporting framework.
  - The accounting policies applied to the group financial statements, changes from those of the previous financial year, and changes resulting from new or revised standards under the applicable financial reporting framework.
  - The procedures for dealing with entities or business units in the group with financial year-ends different from the group's year-end.

### Matters relating to the consolidation process:

- Group management's process for obtaining an understanding of the accounting policies used by entities or business units in the group, and, when applicable, ensuring that uniform accounting policies are used to prepare the financial information of the entities or business units in the group for the group financial statements, and that differences in accounting policies are identified, and adjusted when required in terms of the applicable financial reporting framework. Uniform accounting policies are the specific principles, bases, conventions, rules, and practices adopted by the group, based on the applicable financial reporting framework, that the entities or business units in the group use to report similar transactions consistently. These policies are ordinarily described in the financial reporting procedures manual and reporting package issued by group management.

- Group management's process for ensuring complete, accurate and timely financial reporting by the entities or business units in the group for the consolidation.
- The process for translating the financial information of foreign entities or business units in the group into the currency of the group financial statements.
- How the group's IT environment is organized for the consolidation and the policies that define the flows of information in the consolidation process, including the IT applications involved.
- Group management's process for obtaining information on subsequent events.

Matters relating to consolidation adjustments and reclassifications:

- The process for recording consolidation adjustments, including the preparation, authorization and processing of related journal entries, and the experience of personnel responsible for the consolidation.
- The consolidation adjustments required by the applicable financial reporting framework.
- The business rationale for the events and transactions that gave rise to the consolidation adjustments.
- Frequency, nature and size of transactions between entities or business units in the group.
- The procedures for monitoring, controlling, reconciling and eliminating intra-group transactions and unrealized profits, and intra-group account balances.
- Steps taken to arrive at the fair value of acquired assets and liabilities, procedures for amortizing goodwill (when applicable), and impairment testing of goodwill, in accordance with the applicable financial reporting framework.
- Arrangements with a majority owner or minority interests regarding losses incurred by an entity or business unit in the group (e.g., an obligation of the minority interest to make good such losses).

### **Control Activities**

7. The group auditor's understanding of the control activities component may include matters such as the following:
  - The commonality of information processing controls and general IT controls for all or part of the group.
  - The extent of the commonality of the design of controls for all or part of the group that address risks of material misstatement of the group financial statements at the assertion level.
  - The extent to which commonly designed controls have been implemented consistently for all or part of the group.

**Appendix 3**

(Ref: Para. A110)

### **Examples of Events or Conditions that May Give Rise to Risks of Material Misstatement of the Group Financial Statements**

The following are examples of events (including transactions) and conditions that may indicate the existence of risks of material misstatement of the group financial statements, whether due to fraud or error, including with respect to the consolidation process. The examples provided by inherent risk factor cover a broad range of events and conditions; however, not all events and conditions are relevant to every group audit engagement and the list of examples is not exhaustive. The events and conditions have been categorized by the inherent risk factor that may have the greatest effect in the circumstances. Importantly, due to the interrelationships among inherent risk factors, the example events and conditions also are likely to be subject to, or affected by, other inherent risk factors to varying degree. Also see ISA 315 (Revised 2019), Appendix 2.

<b>Inherent Risk Factor</b>	<b>Examples of Events or Conditions that May Give Rise to the Existence of Risks of Material Misstatement of the Group Financial Statements at the Assertion Level:</b>
Complexity	<ul style="list-style-type: none"> <li>• The existence of complex transactions that are accounted for in more than one entity or business units in the group.</li> <li>• The application of accounting policies by entities or business units in the group that differ from those applied to the group financial statements.</li> <li>• Accounting measurements or disclosures that involve complex processes used by entities or business units in the group such as accounting for complex financial instruments.</li> <li>• Operations that are subject to a high degree of complex regulation in multiple jurisdictions, or entities or business units in the group that operate in multiple industries that are subject to different types of regulation.</li> </ul>
Subjectivity	<ul style="list-style-type: none"> <li>• Judgments regarding which entities or business units in the group require incorporation of their financial information in the group financial statements in accordance with the applicable financial reporting framework, for example, whether any special-purpose entities or non-trading entities exist and require incorporation.</li> <li>• Judgments regarding the correct application of the requirements of the applicable financial reporting framework by entities or business units in the group.</li> </ul>
Change	<ul style="list-style-type: none"> <li>• Frequent acquisitions, disposals or reorganizations.</li> </ul>

<b>Inherent Risk Factor</b>	<b>Examples of Events or Conditions that May Give Rise to the Existence of Risks of Material Misstatement of the Group Financial Statements at the Assertion Level:</b>
Uncertainty	<ul style="list-style-type: none"> <li>• Entities or business units in the group operating in foreign jurisdictions that may be exposed to factors such as unexpected government intervention in areas such as trade and fiscal policy, and restrictions on currency and dividend movements; and fluctuations in exchange rates.</li> </ul>
Susceptibility to Misstatement Due to Management Bias or Other Fraud Risk Factors Insofar as They Affect Inherent Risk	<ul style="list-style-type: none"> <li>• Unusual related party relationships and transactions.</li> <li>• Entities or business units in the group with different financial year-ends, which may be utilized to manipulate the timing of transactions.</li> <li>• Prior occurrences of unauthorized or incomplete consolidation adjustments.</li> <li>• Aggressive tax planning within the group, or large cash transactions with entities in tax havens.</li> <li>• Prior occurrences of intra-group account balances that did not balance or reconcile on consolidation.</li> <li>• Large or unusual cash transfers within the group, particularly to newly incorporated entities or business units operating in locations with a significant or heightened fraud risk</li> </ul>

Indicators that the control environment, the group's risk assessment process or the group's process to monitor the group's system of internal control are not appropriate to the group's circumstances, considering the nature and complexity of the group, and do not provide an appropriate foundation for the other components of the group's system of internal control, include:

- Poor corporate governance structures, including decision making processes that are not transparent.
- Non-existent or ineffective controls over the group's financial reporting process, including inadequate group management information on monitoring of operations and financial results of entities or business units in the group.