The Work of Related Auditors and Other Auditors in the Audit of Group Financial Statements

Comments by
Richard Regal

General Comments
I do not agree with the way that the International Auditing and Assurance Standards Board (IAASB) has dealt with the matter of divided responsibility. The International Accounting Standards Committee (IASC), as it then was, achieved real credibility as a standard setter only when it abandoned its practice of allowed alternative treatments. As the IASC found, allowed alternatives do not help the process of convergence, they hinder it. The IAASB should find it easier to remove this allowed alternative than the IASC did for some of its alternatives. The IASC had to ask countries to adopt treatments that they had previously prohibited or that ran counter to current practice. This would not be the case if the IAASB decided not to allow divided responsibility. I am not aware of any country that requires divided responsibility, only of countries that offer the auditor the ability to choose a method of work that makes divided responsibility appropriate. Those countries still permit sole responsibility audits. On the other side of the argument there are many countries that prohibit joint responsibility audits so making it harder to disallow sole responsibility audits should the IAASB decide that that is the allowed alternative that will have to go. In the context of financial reporting standards, the problems of allowed alternative treatments can be mollified by disclosure, particularly disclosure of the effects of the chosen treatment. This is not possible for auditing standards as there is no mechanism for the auditor to calculate, far less disclose, the effect of using different audit methods.

If the IAASB believes that divided responsibility is a valid operational model, as it must do to permit its use at all, then it should set out clearly the factors that make it particularly appropriate and the circumstances where it would be more appropriate to issue a divided responsibility report or a single responsibility report. The IAASB could then note that in certain jurisdictions divided responsibility reports are not permitted. The wording of the exposure draft, which prohibits it unless allowed by national standards, laws or regulations offers the worst of all worlds. It gives the impression that divided responsibility is not a valid model and makes the determination of what is an audit in accordance with International Standards on Auditing (ISAs) subservient to national standard setters.

The IAASB has the sole jurisdiction for deciding what is an audit in accordance with ISAs; a jurisdiction that is not subject to any national body for court. National rules can decree that certain procedures are not necessary for an audit in accordance with national standards but an audit so conducted is not an audit conducted in accordance with ISAs. If the IAASB should wish to remove the division of responsibility option it can do so. Auditors in countries that allow it then have a clear choice of conducting their audits to comply with both international and national standards or conducting their audits to comply with national standards only.

Furthermore, the manner in which the exposure draft is currently written does not make it easy for the standard to be applied consistently. Most countries that allow divided responsibility reporting allow it for all audits, not just for group audits. The exposure draft allows it only for group audits. Why? If divided responsibility is acceptable at all then it is surely acceptable for all audits. If the sole decision as to whether divided responsibility is to be allowed is a decision that is left to national standard setters then the IAASB should not restrict its use to group audits unless
national standards do. There is also the problem that not all countries necessarily allow or prohibit divided responsibility in the same circumstances. Country A might prohibit divided responsibility, Country B might prohibit it in all but certain circumstances and Country C might prohibit it in all but certain circumstances that are different from those in which country B allows it. An auditor working and reporting in Country C might know that the report will be circulated in Countries A and B but will presumably use Country C’s rules for determining the question of divided responsibility. If the auditor issues a divided responsibility report what are the readers in countries A and B to make of it? Readers in country A, who are unused to divided responsibility reporting, will look first to the ISAs (because the audit report will say the audit has been conducted in accordance with ISAs) and find nothing. If they look harder they will find a reference to the auditor following national standards and so might investigate the auditing standards of Country C. The reader in Country B is even worse off. Being used to divided responsibility reports he is likely to assume that the conditions for their application in ISAs are similar to the conditions for their application in national standards. Such confusion can surely not be in the interests of convergence.

National standards may use the current wording of the exposure draft in such a manner that allows auditors to exempt themselves from the requirements of ISAs and yet still say that they have conducted an audit in accordance with ISAs or in a way that allows auditors to avoid issuing a limitation of scope qualification. For example, one country permits (indeed, encourages) a divided responsibility report in circumstances where it may be impracticable for the group auditor to review the other auditor’s work or use other procedures to satisfy himself as to the work performed by the other auditor. It seems to me that the proper response to such circumstances is for the auditor to issue a qualified opinion (or for him not have accepted the audit in the first place) rather than to allow the auditor to issue an unqualified opinion and merely indicate in the report that he has not fully audited certain parts of the financial statements.

The standard does not deal with how the reader of a divided responsibility audit report will satisfy himself as to the nature of the work done on the portions of the financial statements that the group auditor has not audited. There is no indication as to whether those portions have been audited at all and if so whether that audit has been conducted in accordance with ISAs. In such circumstances I think it would be a travesty if the group auditor’s report were to indicate that the audit of the group’s financial statements had been conducted in accordance with International Standards on Auditing when parts of the same report indicated that it has not been.

The standard as currently drafted means that in a divided responsibility audit the following black letter requirements that have no relevance to the shifting of responsibility are no longer black letter requirements:

(a) considering whether the group auditor’s involvement is sufficient to be able to act as the group auditor;

(b) considering the professional qualifications, independence, professional competence and resources of the other auditor; and

(c) determining the audit procedures to be performed on the consolidation.

It seems to me that as the group auditor is still responsible for the opinion on the group financial statements as a whole then these should remain black letter requirements even for divided responsibility audits. Similarly the drafting means that the following requirements are also no longer black letter requirements for divided responsibility audits even though very strong arguments could be advanced for making them so:
(a) communicating the group auditor’s requirements to the other auditor; and

(b) considering whether the findings of the other auditor have an effect on the report on the group financial statements.

It would be possible for the standard to be drafted in such a way that national standards determined whether, and the extent to which, it was possible to use divided responsibility reporting and ISAs determined the work the group auditor should do on a divided responsibility audit. Whilst I do not think that that would be particularly desirable, it would at least allow for consistency in the application of ISAs to group audits.

The document is inconsistent in its use of “related auditor or other auditor” and “related auditor and other auditor”, sometimes using one construction, sometimes the other and sometimes refers to them in the singular and sometimes in the plural. I draw attention to the differences between the headings above paragraphs 25 and 29 and the inconsistency between the heading above paragraph 29 and the words of paragraph 29. I believe it would also be helpful if the document could use a generic term for “related auditor or other auditor” as this would save some very cumbersome drafting. I suggest the term “secondary auditor”, although I realize this could give some problems with divided responsibility audits.

The document uses “impacted” when “affected” and would be a more appropriate word to use. It also uses “impact” when a more appropriate word is either “affect” or “effect” depending on whether “impact” is used as a verb (for example, the first time it is used in paragraph 33) or a noun (for example, the second time it is used in paragraph 33). (I believe the only time it is used as a verb is in paragraph 33, which should make editing by a global search and replace fairly easy.) I do not suggest that many people translating the document will be fooled by the first dictionary definition of “impact” but I do think that the IAASB should avoid making things unnecessarily difficult for translators by its use of English.

**Specific Comments**

Paragraph 2 states that the group auditor is responsible for expressing an opinion on the group financial statements and for determining the work to be performed on the component financial information. However, this is not true in the case of a divided responsibility audit. In such an audit the group auditor’s report states that the group auditor has not audited all of the financial statements and that a portion of the financial statements have been audited by someone else.

The penultimate sentence of paragraph 4 implies that the only case of combined financial information that is not group financial information is where a parent does not exist. Is that intended, or should the “i.e.” be an “e.g.”?

Paragraph 5 is an abdication of the IAASB’s responsibility to set International Standards on Auditing. I can see no justification for allowing a national standard setter to override what is required for compliance with ISAs. For example, paragraph 22 of ISA 570, “Going Concern” does not say, “Unless permitted not to by national standards the auditor should inquire of management as to its knowledge of events or conditions beyond the period of assessment used by management…” but rather, “The auditor should inquire of management as to its knowledge of events or conditions beyond the period of assessment used by management…” . If the IAASB believes that divided responsibility is acceptable then it should allow divided responsibility in all cases and should note that some jurisdictions restrict auditors’ ability to divided responsibility. In
other words the bold letter part of the paragraph should be rewritten as follows.

The group auditor may take sole responsibility for the audit opinion on the group financial statements or, unless national legal requirements dictate otherwise, may divide responsibility for the audit opinion on the group financial statements (referred to as "division of responsibility"). **When the auditor takes sole responsibility for the audit opinion on the group financial statements the group auditor should not refer to the other auditor in the auditor’s report on the group financial statements except as provided for in paragraph 31.**

It would also be helpful if the IAASB gave some guidance as to when it believed divided responsibility was more appropriate than sole responsibility and when it believed sole responsibility was more appropriate than divided responsibility.

Although the IAASB clearly believes that divided responsibility is an acceptable approach to audits of group financial statements, I do not. The standards based on the new audit risk model require the group auditor to obtain an understanding of the [group] and its environment sufficient to design and perform further audit procedures. The group auditor is required to make risk assessments at the group financial statement and assertion levels and to design and perform audit procedures in response to those risks. The standards allow the performance of audit procedures to be delegated to others but they in no way allow the responsibility for their performance to be delegated. Whatever arguments there may have been for permitting divided responsibility audits under the previous risk model there does not seem to be any justification for its retention under the new audit risk model. Furthermore, national standards that currently permit divided responsibility reporting were written with the old audit risk model in mind. The IAASB cannot be sure that the national standards in every country that permits divided responsibility reporting impose conditions or requirements that make sense when applied to the new audit risk model.

I believe that the time has come when the IAASB has to make a firm decision: it cannot duck the issue much longer. I believe that it should make good on the statement in paragraph 2 and no longer allow the auditor to divide responsibility in audits conducted in accordance with International Standards on Auditing. An auditor who wishes to divide his or her responsibility can do so under national auditing standards, but then the auditor’s report should have to refer to compliance with national auditing standards only and not to compliance with ISAs.

However, if the IAASB continues to allow divided responsibility reporting then since paragraph 37 makes paragraphs 8 and 9, and 15 to 17 apply to both sole responsibility audits and joint responsibility audits I believe it would be helpful to move paragraphs 15 to 18 above paragraph 10. This would allow the last sentence of paragraph five to be rewritten to make it clearer which paragraphs apply to which types of audits. The sentence could then be rewritten as follows, “The standards and guidance in paragraphs 7 to 13 apply to all audits. The standards and guidance in paragraphs 14 to 34 apply when the auditor takes sole responsibility for the audit opinion on the group financial statements and the standards and guidance in paragraphs 35 to 41 apply to audits where there is divided responsibility for the audit opinion on the group financial statements.”. This would allow the first sentence of paragraph 6 to be deleted.

I am not sure what purpose is served by paragraph 6. The first sentence belongs more naturally with the previous paragraph and the third (final) sentence merely repeats what is in paragraph 5. This leaves the second sentence, in which the IAASB seems to restrict the ability of national standards to define when divided responsibility applies. The IAASB cannot have its cake and eat it. Either national standards define whether and when divided responsibility can be used or the ISAs do. If the IAASB wants place restrictions on the allowability of divided responsibility reporting
then it should develop its own guidance on the applicability of divided responsibility. Also, as a matter of style, the IAASB should adopt a consistent way of referring to blocks of paragraphs: either paragraphs 7 to 34 (as in paragraph 5) or 7–34 (as in this paragraph).

Paragraph 7(h) picks up the definition of network firm from the quality control standards. I do not believe that people commenting on those standards and the definition of the term therein (or those commenting on the proposed revision to the code of ethics) did so realizing that the term would be used so liberally in relieving auditors from the requirements of other ISAs.

In paragraph 8(b) the word “include” should be changed to “give rise to”. The group auditor is considering the group financial statements and so the important point is not whether a component itself includes risks (of material misstatement of the parent’s financial statements) but rather how the component’s existence affects the risks of such a misstatement (which includes but is wider than the risks in the component itself). ISA 315, “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement” sets the definition of “significant risks” as risks that in the [group] auditor’s judgement “require special audit consideration”. It seems to me therefore that if there are any significant risks associated with a component then the group auditor must be the person that has audit responsibility for that component in order to ensure that the group auditor considers all the risks of misstatement that require special audit consideration. This would seem to make divided responsibility reporting difficult to achieve in practice. If the standards are to be followed the group auditor will have to make a separate determination each year as to whether a component can be dealt with under divided responsibility and that determination can be made only after that year’s assessment of the risks of material misstatement. However, in practice, the arrangements for who is going to audit what components are usually made at the start of the audit.

Paragraph 8(e) should refer to “auditors” in the plural (and “other auditors’ working papers”) to be consistent with the remainder of the paragraph.

In the first sentence of paragraph 9, the words “appears to be” should be replaced by “is” or else the words “resolve the insufficiency” should be replaced by “rectify the apparent insufficiency”. In the fourth bullet point, I do not see how the group auditor can participate in the other auditor’s evaluation of audit evidence. Evaluation is a mental process that the other auditor undertakes. The group auditor might perform his or her own evaluation (or re-evaluation) but is not taking part in the other auditor’s evaluation when he or she does so.

I find the first sentence of paragraph 14 difficult to comprehend. It appears to be saying “The fact that a component’s financial statements are subject to audit may affect the group auditor’s decision on the work to be performed on the component’s financial information for the purpose of the audit of the group financial statements.”. If so, I suggest that it be rewritten as above.

Paragraph 15 requires the group auditor to consider various factors relating to the other auditor. Paragraphs 16 and 17 give various sources of information for that consideration, including representations from the other auditor. However, no mention is made of the need to check the representations to be satisfied that they are accurate.

In the first sentence of paragraph 21, “communicate to” should be “communicate with” as there will be two-way communication rather than one-way communication (at the very least the other auditor will need to communicate that he or she has understood the requirements). The second, third fourth and fifth bullet points should each be preceded by the word “That” to fit in
grammatically with the sentence that introduces them. Also the third, fourth and fifth bullet points do not say what the other auditor’s understanding should be sufficient for. For example, the fourth bullet point should say something to the effect of “That the related auditor or other auditor has a sufficient understanding of the financial reporting framework and other statutory requirements applicable to the group financial statements to enable the related auditor or other auditor to identify matters that need to be brought to the attention of the group auditor.”.

The second sentence of paragraph 22 is difficult to comprehend. It should be rewritten as follows.

The communications from the related auditor or other auditor include the acknowledgements and confirmations referred to in paragraph 21 and a report on the work that the related auditor or other auditor has carried out. The communications referred to in paragraph 21 are obtained before the related auditor or other auditor commences work on the components financial information. The report on the work carried out is obtained at the date of conclusion of the work of the components financial information and…

Paragraph 29 seems to be written the wrong way round in that there is no requirement to consider the findings of the related auditor or other auditor to see whether there are any matters that may affect the group auditors report. I think the sentence should be rewritten as “The group auditor should consider whether the findings of the related auditor or other auditor may have an effect on the auditor’s report on the group financial statements.”.

The bold letter sentence in paragraph 35 is incomplete. As written it seems to imply that if the group auditor decides to divide responsibility then the entire audit follows relevant national standards (rather than ISAs). This cannot have been the IAASB’s intent. As stated above, I believe that the IAASB should not allow division of responsibility and that if it does allow it should make its own rules for when division of responsibility is appropriate. However, if the IAASB does want to cede to national standard setters some ability to decide what constitutes an audit in accordance with ISAs then it should state clearly the areas where national standards will determine the requirements.

I am not sure what purpose paragraph 36 serves. If the IAASB has decided that national rules determine when division of responsibility is (and therefore when it is not) appropriate, it cannot create its own additional rules saying when division of responsibility is appropriate.

It is not clear to me how paragraph 39 is meant to operate. In a divided responsibility audit the group auditor is not using the work of the other auditor as a basis for the opinion on the parts of the financial statements for which the group auditor is not accepting responsibility. I do not, therefore, see how there can be circumstances where the group auditor is not accepting responsibility for the work of other auditor whilst the same time basing an opinion on that other auditors work.

Paragraph 37 and paragraph 41 combined leave me confused as to what the black letter requirements are in a divided responsibility audit. Paragraph 5 implies that neither the definitions in paragraph 7 nor the standards in paragraphs 8 to 34 apply. Paragraph 37 implies that some of the work required by those standards will ordinarily be carried out but does not make that a black the requirement nor are there any imperatives in the drafting. However, paragraph 41 requires the documentation of one of the procedures mentioned in paragraph 37 and the documentation of two procedures that paragraph 37 does not mention.
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The Audit of Group Financial Statements

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General Comments

As currently drafted an auditor who departs from the practice statement would have to be prepared to explain how the requirements in the International Standards on Auditing (ISAs) that this practice statements address have been complied with if he or she issues a sole responsibility report but not if he or she chooses to take advantage of national standards that allow divided responsibility reporting. This seems illogical considering that the practice statement addresses the requirements of ISAs that apply equally to divided responsibility and sole responsibility audits (for example, paragraphs 22 to 27 deal with the application of ISAS 610, “Considering the Work of Internal Audit”, a standard that applies to all audits). Furthermore, even the guidance that relates only to ISA 600, “The Work of Related Auditors and Other Auditors in the Audit of Group Financial Statements” deals with aspects of that standard that are applicable (or should be made applicable) to both types of audit. I do not believe the application of the International Auditing Practice Statement (IAPS) should be limited to sole responsibility audits but that it should also apply to those audits where the auditor chooses a way of conducting the audit that renders the issue of a divided responsibility audit report necessary or desirable.

The IAASB is producing this practice statement because it believes auditors need guidance on how to apply the ISAs to group audits. It surely cannot believe that an auditor who needs guidance on how to apply ISAs to a sole responsibility group audit will not need guidance on how to apply ISAs to a divided responsibility group audit. Similarly, it cannot believe that regulators or other users of audit reports need something to help them understand what is expected in a sole responsibility group audit but do not need anything to help them understand what is expected in a divided responsibility group audit. It seems to me that the IAASB is not itself sure about how divided responsibility reporting fits in with the recent fundamental changes to the audit standards, and that is why it is unable or unwilling to produce such guidance. This might indicate that the time has come for the IAASB to drop its acceptance of divided responsibility reporting, a practice that arose in the days when auditors and audit standards adopted an approach to auditing that was based more on substantive testing of transactions and balances and less on understanding the entity and its environment.

I believe it would be helpful if the document could use a generic term for “related auditor or other auditor” as this would save some very cumbersome drafting. I suggest the term “secondary auditor”.

Although I do not feel strongly on the matter, I believe that it is generally unhelpful to include diagrams in standard setting documents. For example, paragraph 58 states that an audit is ordinarily (but not always) performed on the financial information of components that encompass a large (but not necessarily significant) proportion of the group’s operations. The diagram that precedes this paragraph implies that an audit is always carried out but only on components of individual financial significance (irrespective of the proportion of the group’s operations they represent). It this difficulty of ensuring that the diagram is unlikely to be interpreted differently from the text that makes me suggest that the diagram be omitted. Diagrams risk oversimplifying complex subject matters, thereby not including all factors that the main text contains. This then leads to the impression that an item not mentioned in the diagram is of secondary importance and
also means that many people will base their understanding of the document on the diagram rather than the text.

The document uses “impacted” when “affected” and would be a more appropriate word to use. It also uses “impact” when a more appropriate word is either “affect” or “effect” depending on whether “impact” is used as a verb or a noun. I do not suggest that many people translating the document will be fooled by the first dictionary definition of “impact” but I do think that the IAASB should avoid making things unnecessarily difficult for translators by its use of English.

**Specific Comments**

The penultimate sentence of paragraph 4 implies that the only case of combined financial information that is not group financial information is where a parent does not exist. Is that intended, or should the “i.e.” be an “e.g.”?

Paragraph 8 is a new departure for the IAASB. Previously, definitions used in an IAPS were defined in the body of the IAPS and a glossary was used to explain any technical terms. This, for example, was the practice adopted in IAPS 1012, “Auditing Derivative Financial Instruments”, where necessary definitions were built into the text. I believe that the same approach should be followed for this IAPS.

Paragraphs 11, 12 and 13 use unusual phrasing for a document is meant to provide guidance on the application of standards. It is perfectly acceptable, and indeed proper, for a document that merely describes how auditors work to include phrases such as “in most cases the auditor will wish” and “it will be unusual for the auditor to”. However, this document is meant to provide guidance for auditors and if auditors depart from its guidance they have to be prepared to justify that departure (and courts will surely ask them to do so). In that context, is doing something that is unusual a departure or not; is failing to do something that is done in most cases a departure or not? The wording of the exposure draft could make it difficult for auditors to defend themselves in circumstances where it was not intended to do so.

I think paragraph 13 could be improved if the correction for the unusual circumstance was placed next to the definition of the unusual circumstance. Also the words “include significant risks” should be changed to “give rise to significant risks”. The group auditor is considering the group financial statements and so the important point is not whether a component itself includes risks (of material misstatement of the parent’s financial statements) but rather how the component’s existence affects the risks of such a misstatement (which includes but is wider than the risks in the component itself). The sentence should therefore read as follows. “Where components have been identified at the group level as likely to give rise to significant risks of material misstatement of the group financial statements it will be unusual for a group auditor to accept an engagement where those components are audited by other auditors unless the group auditor will be able to participate appropriately in the work to be performed by the other auditors on those components’ financial information.” However, even that construction is somewhat clumsy (and like the version in the exposure draft refers at one point to the component as being the subject of the audit rather than its financial statements). I would therefore suggest the following. “Some components may have been identified at group level as likely to give rise to significant risks of material misstatement of the group financial statements. It would be unusual for a group auditor to accept an engagement if the work to be performed on such components’ financial information is to be performed by other auditors unless the group auditor will be able to participate appropriately in the work.” Of course, that still leaves open the question of whether an IAPS should use the term
“unusual” or whether the second sentence should start “A group auditor does not ordinarily accept an engagement...”.

In paragraph 17, “specifies” should be “specify”.

In paragraph 38, I do not think that it is right to allow the group auditor to substitute a related auditor’s understanding for his or her own understanding. If it is acceptable then it should be acceptable to allow him or her to substitute the understanding of another auditor, not just a related auditor. The distinction between a related auditor and another auditor is based upon whether or not the auditor is part of the same network as the group auditor as defined for quality control purposes. That distinction surely has no significance for the group auditor’s ability to substitute a different auditor’s thought processes for his or her own. If the group auditor has identified components as giving rise to risks that require special audit consideration then the group auditor him or herself should obtain an understanding of those components as they affect the group financial statements and should not relay on somebody else’s understanding even if that person is part of the same quality control network.

In paragraph 39, all the bullet points in the first block should be preceded by the word “the” as should the third and fourth bullet points in the second block. The first bullet point in the third group (matters relating to consolidation adjustments) is “Business rationale for consolidation adjustments”. Consolidation adjustments are generally required by the financial reporting framework (for example, the writing off of goodwill on acquisition). The business rationale does not enter into matters unless one is talking about the business rationale for the transactions that give rise to the consolidation adjustments.

The last sentence of paragraph 45 can be rewritten to avoid the use of bullet points as follows. “In the case of an audit of group financial statements there may also be discussions that involve the group auditor and related auditors and other auditors or key members of those auditors’ teams.” However, a better solution would be to find a generic term for auditors other than the group auditor.

Paragraph 46 states that the group auditor may consider it appropriate to participate in the risk assessments of related auditors and other auditors. I do not see how the group auditor can participate in another auditor’s assessment of risk. Risk assessment is a mental process that the other auditor undertakes. The group auditor might perform his or her own assessment (or reassessment) but is not taking part in the other auditor’s assessment when he or she does so.

In paragraph 47, the semicolons at the end of the bullet point should be full stops and the “and” at the end of the penultimate bullet point should be deleted. I am also not sure what is meant by “address the application of the applicable financial reporting framework to the components’ facts and circumstances”. Presumably the applicable financial reporting framework referred to is that used for the group financial statements. If that is the case and if the components’ financial information has not been prepared using that framework then what is being discussed is the need for appropriate consolidation adjustments. In any event, the requirement itself is unusual. I am not sure where, in an audit of single entity financial statements, the auditor’s addressing of the application of the applicable financial reporting framework to the entity’s facts and circumstances is discussed in the ISAs or other IAPSSs.

Paragraph 48 refers to the other auditors having a sufficient understanding without saying what that understanding should be sufficient for. I suggest that the sentence should read, “…that they
have a sufficient understanding of the financial reporting framework and other statutory requirements applicable to the group financial statements to enable them to identify matters that need to be brought to the attention of the group auditor.”

In paragraph 50 the second bullet point should refer to “an inadequate flow of management information”, and the third bullet point to “group-wide controls that do not, in fact, exist or that are not operating effectively”. The third bullet point should be two points, with the split coming after “exchange rates”. The penultimate bullet point refers to the possibility that different financial year-ends may be used to manipulate the timing of transactions. The manipulation of timing has more to do with fraud, and should be mentioned as part of the consideration of fraud risk factors. Its inclusion here leads to the implication that the only source of misstatements caused by different year-ends is the manipulation of timing, which is not the case. I suggest that the words after the comma be deleted and that the consideration of the manipulation of timing of transactions in connection with different year-ends be moved to the parts of the document dealing specifically with fraud.

I am not sure why the word “especially” is used in paragraph 51. The point is equally important in the audit of single entity financial statements, and that particular type of misstatement is no more important than any other.

The heading above paragraph 53 introduces to the language the verb “to scope”. The IAASB does not usually adopt shorthand phrases, preferring to use full forms were possible, and I do not see why it has suddenly changed its habit here. I suggest that the heading be changed to “Determining the Scope of Work to Be Performed on the Components’ Financial Information”.

In the second bullet point of paragraph 55, I suggest that “specified audit procedures” should read “specified procedures”. This would help to avoid giving the impression that specified procedures could ever amount to an audit in their own right.

The first sentence of paragraph 56 seems to be a long-winded way of saying “The fact that a component’s financial statements are subject to audit may affect the group auditor’s decision on the work to be performed on the component’s financial information for the purpose of the audit of the group financial statements.” I also believe that after the sentence “The group auditor may decide that it is efficient and cost-effective to use the audit evidence obtained in the audit of the component’s financial statements for the purposes of the audit of the group financial statements.”, the following sentence should be added. “However, the group auditor bears in mind that the auditor of the component will not have considered the risk of material misstatements in the group’s financial statements when performing the audit of the component’s financial statements.” If this addition is accepted, the “However,” that precedes the next sentence should be deleted.

Paragraph 58 states that an audit is ordinarily (but not always) performed on the financial information of components in certain circumstances. However, it is a rather unusual audit in that the determination of materiality is not left to the auditor of the information but is made by somebody else and is likely to be a much higher level than an auditor of just that information would set for him or herself. In addition, an audit of the financial information will not produce all the audit evidence that the group auditor requires. An audit of financial information is based on the assessment of risks of material misstatement of that information: it is not based on the assessment of risks of material misstatement of other information. It is quite possible that for complex groups the nature or purpose of the component may give rise to risks of material misstatement arising in the group’s financial statements without there necessarily being an
equivalent risk of material misstatement arising in the components’ own financial information. This may occur, for example, when risks arising in different components interact with each other in ways that lead to higher combined risks for the group than exist in the individual components (a sort of reverse synergy). An audit of the component’s financial information (in the usual meaning of the term “audit”) will not pick up the fact that risks that are not significant risks when looked at from the viewpoint of the component’s financial information may be a significant risk when looked at from the viewpoint of the group’s financial statements. This paragraph and the diagram oversimplify this point.

In paragraph 67, the object to which the word “it” refers is not clear; grammatically it must refer to a noun, but the most likely nouns are either “group management” or “the group auditor”. I believe it is meant to refer to management’s insistence. The sentence should be reworded as follows. “Group management might request the group auditor to perform less work on a component’s financial information than the group auditor believes appropriate. If the group auditor agrees to do so then that will be a limitation of the group auditor’s scope and the group auditor considers the effect of the limitation on the report on the group financial statements.”

I believe the first sentence of paragraph 69 should be split into two sentences as it is extremely long. It also contains the novel verb “to scope”. Assessments and determinations do not include expectations although they may be based on them (or assumptions). I believe the sentence should be rewritten as follows. “The group auditor’s risk assessment at group level and the group auditor’s determination of the scope of work to be performed on the components’ financial information may be based on an expectation that group-wide controls are operating effectively. Where there is such an expectation, the group auditor performs, or requires...”.

Paragraph 70 also contains the novel verb “to scope” and I believe should be rewritten as follows. “The group auditor, related auditors and other auditors perform the work on the components’ financial information in accordance with the group auditor’s determination of the scope of work based on the risk assessment that the group auditor performed at group level.”

Paragraph 71 (and indeed the whole area of consolidation) is one of the subjects that most obviously applies equally to divided responsibility and sole responsibility audits and reveals how badly needed is an IAPS that applies to divided responsibility audits. The paragraph refers to formal journal entries, and I am left wondering how there can be informal journal entries. (Indeed, in today’s computerised age many people may be left wondering what journal entries, formal or informal, are.) In addition, the construction of the first sentence makes it difficult to determine what it is that is not reflected in the journal entries, I think it is the adjustments to the amounts reported. I also believe the sentence has an undue emphasis on fraud since consolidation adjustments are error prone at the best of times and by concentrating on fraud the auditor may fail to detect misstatements that arose through simple error. It would be helpful if the paragraph used the same terminology that is used in ISA 315, “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement”. I believe the first sentence should read as follows. “The consolidation process may require adjustments to amounts reported in the group financial statements that do not pass through the usual transaction processing systems and that may not be subject to the same internal controls that other financial information is subject to. These adjustments typically comprise consolidation adjustments and reclassifications.”

I do not think there is a great need to give examples of the other ISAs in paragraphs 80 and 87 unless there is something particularly special about that particular ISA.
This IAPS deals with how to apply many ISAs, not just ISA 600. For example, it deals with how the auditor applies ISA 315. I therefore think the effective date in paragraph 91 should not be linked to the effective date of ISA 600 but rather to the effective dates of the standards on which it gives guidance. Indeed, I do not believe that IAPSS ought to have effective dates, since they do not set any new requirements at all. However, if it is desired to give IAPSS effective dates then I believe the wording should be along the following lines. “Auditors should be prepared to explain how the requirements in the standards addressed by this practice statement have been complied with in respect of audits of financial statements for periods ending on or after [date] or such later effective date as the standards addressed by this practice statement are effective.”

In appendix 2, the required acknowledgements and confirmations should indicate what the understanding required of the other auditor should be sufficient for. The first three bullet points relating to “other information” should be in the subjunctive mood: “a request that a list be provided”, “a request that the following be reported” and “a request that the group auditor be notified”.

In appendix 3, the word “it” is an odd word to use to describe an auditor, and I believe should be replaced with the words “the auditor”. There is also a missing “of” after the words “true and fair view” in the first paragraph of the specimen letter.