

# HONG KONG SOCIETY OF ACCOUNTANTS

(Incorporated by the Professional Accountants Ordinance, Cap. 50)

**By e-mail < [EDComments@ifac.org](mailto:EDComments@ifac.org) > and by fax (0062 1 212 286 9570)**

Our. Ref.: C/AASC

21 April 2004

Technical Director,  
International Auditing and Assurance Standards Board,  
International Federation of Accountants,  
545 Fifth Avenue, 14<sup>th</sup> Floor,  
New York,  
New York 10017,  
USA.

Dear Sir,

**IAASB Exposure Draft on ISA 600 (Revised) “The Work of Related Auditors  
and Other Auditors in the Audit of Group Financial Statements”  
and IAPS “The Audit of Group Financial Statements”**

The Hong Kong Society of Accountants welcomes the opportunity to provide you with our comments on the captioned IAASB Exposure Draft.

--- We set out in the attachment our comments for your consideration.

We trust that our comments are of assistance to you. If you require any clarifications on our comments, please contact the undersigned at [schan@hksa.org.hk](mailto:schan@hksa.org.hk).

Yours faithfully,



STEPHEN CHAN  
TECHNICAL DIRECTOR (ETHICS & ASSURANCE)

SSLC/SO/jc  
Encl.

**HONG KONG SOCIETY OF ACCOUNTANTS' COMMENTS ON THE IAASB  
EXPOSURE DRAFT ON ISA 600 (REVISED) "THE WORK OF RELATED AUDITORS  
AND OTHER AUDITORS IN THE AUDIT OF GROUP FINANCIAL STATEMENTS"  
AND IAPS "THE AUDIT OF GROUP FINANCIAL STATEMENTS"**

**SIGNIFICANT COMMENTS**

**1. Division of responsibility – Paragraph 5 of proposed revised ISA 600**

We do not agree with the idea of divided responsibility for the audit opinion on the group financial statements and do not support the proposed changes to ISA 600 that elevate the option of divided responsibility with other auditors as an equally valid alternative approach for the following reasons:

- We cannot see how divided responsibility becomes acceptable under ISAs where national standards allow this approach, if divided responsibility is considered inappropriate in most jurisdictions worldwide (notable exceptions being the United States, Italy and some South American countries).
- We understand the reason the IAASB has retained divided responsibility is to accommodate jurisdictions that allow this approach in their national standards. We fail to see the logic of this, as jurisdictions that wish to retain this approach within their own standards are not prevented from doing so by an ISA that lays down an obligation for sole responsibility when applying ISAs.
- By allowing divided responsibility, the IAASB appears to be abrogating its responsibilities to set appropriate standards. This is not an appropriate message to send at a time when audit work is attracting highly critical comments on the precise topic of audits involving divided responsibility for the audit opinion on the group financial statements.
- The group auditor has a responsibility to form an opinion on the group financial statements as a whole and therefore needs to obtain sufficient appropriate evidence on which to form that opinion. In a risk-assessment approach to the audit, it is important to obtain a sufficient understanding of the group as a whole in order to properly assess risks in that group audit. It may be difficult to obtain that information or understanding if the group auditor is simply relying on the other auditor's work.
- An opportunity to commit fraud may more readily arise when the entity is able to divide auditors between components of the group.

If despite our strong objection divided responsibility is retained, we believe that there should be prominent disclosure regarding the identity of the other auditors as well as the information as to the portion of financial statements audited by these auditors. This information would as a minimum provide the name, place of operation and qualification of the auditors. Where there are many other auditors the full details need only be provided for those responsible for significant portions of the financial statements not under the responsibility of the group auditor.

## **SPECIFIC COMMENTS ON PROPOSED REVISED ISA 600**

### **2. The Group Auditor and the Related Auditor – Paragraphs 7(h), 8 and 18**

We consider that the subject paragraphs need further consideration and clarification as follows:

- (a) We note that paragraph 7(h) has defined “Related auditor” to mean an independent auditor from the group auditor’s office, other office of the group auditor’s firm, a network firm or another firm operating under common quality control policies and procedures as described in ISQC 1. We question how a firm that operates under common quality control policies would not fit under the idea of a network firm.
- (b) Paragraph 8 clearly distinguishes between work done by related auditors and that done by other auditors. It allows the auditor to treat work done by related auditors as being part of what we might call the auditors’ “wider firm”. Later in paragraph 18 a reference is made to common procedures in many other areas like recruitment, training, advancement, auditor independence, audit methodology and quality control. This clearly shows that the IAASB has had to develop the idea of a related auditor to paper over the cracks in the IFAC Ethic Code definition of a network firm. We suggest that the IAASB would need to go the whole way and say that the ethical obligations on network firms also apply to any firm that for a particular engagement is treated as a related auditor. We would also recommend that the IAASB liaise with the IFAC Ethics committee to revise the definition of the network firm.
- (c) The mandatory procedures in paragraph 8 require that the group auditor is obliged to consider whether his involvement is sufficient to be able to act as group auditor. While we note it is implied that if the answer is “no” the auditor should not accept the engagement, we would recommend that this needs to be made explicit in paragraph 8 rather than merely stating it explicitly in paragraph 15 of the proposed IAPS.
- (d) The definition of related auditor in paragraph 7(h) only requires the group auditor and the related auditor to share common quality control procedures. Paragraph 18 refers to reliance on common procedures over a much wider range of matters as mentioned above. The definition in paragraph 7(h) needs to be updated to cover these factors or paragraph 18 should make it clear that before relying on common traits the group auditor needs to take steps to satisfy himself that these are in fact common.

### **3. Compliance with ISQC 1 – Paragraphs 15 to 17**

The mandatory procedure requires the group auditor to consider the quality control process of the other auditor’s firm. The guidance in paragraph 17 states that with regard to quality control process the group auditor obtains a representation that the other auditor complies with ISQC1. It implies the only procedure relating to quality control process of another auditor is to obtain the representation. We do not consider that the obligation to consider the quality control process can be satisfied by only obtaining a representation. Paragraph 17 should be amended to clarify that the representation is only part of the overall process. The enquiries and questionnaire referred to in paragraph 16 will cover the issue of the quality control process.

4. **Concluding on the qualification of other auditors – Paragraphs 15 and 34**

Paragraph 15 of the ISA requires the group auditor to consider the professional qualifications, independence, professional competence and resources of the other auditor, and the quality control process of the other auditor’s firm in the context of the work to be performed by the other auditor. The ISA refers to sources from which the group auditor might obtain information about the other auditor (e.g. professional bodies, licensing bodies, professional colleagues, direct representation or references from third parties). It also says that the group auditor obtains a representation that the quality control processes of the other auditor’s firm comply with the proposed ISQC 1. Whilst we agree with this guidance, in the documentation requirements in paragraph 34 of the proposed revised ISA 600, the group auditor is required to document a conclusion with regard to such observations. In our view, while the group auditor can perform the procedures suggested and document the results of those procedures, including any concerns regarding any of the matters and how the group auditor has responded to those matters, it may be difficult for the group auditor to conclude definitively about the other auditor’s “qualifications”.

We suggest that the proposed revised ISA 600 offer further clarification on the type of documentation expected with regard to the other auditor’s qualifications. Alternatively, it may be more appropriate to document what evidence has been obtained instead of having to conclude definitively.

5. **Access to Information – Paragraph 20**

The mandatory procedure requires that when there are restrictions on the group auditor’s access to component information, component management or related auditors or other auditors, including their working papers, and if this difficulty cannot be resolved through group management or other means, the group auditor should consider the impact of this scope limitation on the auditor’s report on the group financial statements. We consider that this does not go far enough. This is because the group auditor should consider not only the impact of the scope limitation on the auditor’s report but also whether the restrictions call into question the basis of preparation of the group financial statements. Failure by group management to procure sufficient access by the group auditor may indicate that there is insufficient control or influence for the entity to be considered as a subsidiary or an associated company under the financial reporting framework.

6. **Acknowledgement of the other auditor’s understanding – Paragraph 21**

The mandatory procedure requires the group auditor to communicate to the related auditors and other auditors to provide them with the group auditor’s requirements and the guidance mentions that in the case of an other auditor, an acknowledgement of the other auditor’s understanding that the group auditor intends to consider and use the other auditor’s work for purposes of the audit of the group financial statements be obtained. We question why the acknowledgement that the group auditor will rely on the work of the other auditor is not obtained from related auditors.

7. **Mandatory review of working papers – Paragraphs 25 and 27**

The mandatory requirement in Paragraph 25 states that the “group auditor should determine whether the work of the related auditor or other auditor is adequate for the group auditor’s purposes in the context of the audit of the group financial statements”.

We interpret the above paragraph as suggesting that the nature and extent of the review of working papers should be based on judgement. We agree with this approach. However, the guidance in paragraph 27 goes beyond the bold-lettered principle as it is quite definitive; suggesting that where the group auditor does not participate in the work performed by other auditors on significant financial components then the group auditor reviews, or requires that a related auditor to review, other auditor's working papers. We would suggest that the guidance be less definitive on the need to always review the other auditor's working papers. Instead the guidance should be expanded to recognize the range of procedures that might be performed to obtain evidence with respect to the adequacy of another auditor's work for the group auditor's purposes. Whether review of working papers is necessary, and the nature and extent of any review, depends on the circumstances, including other procedures the auditors may have performed to be satisfied with respect to the quality of the work performed by the other auditor.

## **SPECIFIC COMMENTS ON PROPOSED NEW IAPS**

### **8. Paragraph 12**

This paragraph suggests that it will be unusual for a group auditor to accept an engagement to audit group financial statement where the group auditor and related auditors directly perform work "on less than approximately 50%" of the group assets, liabilities, cash flows, profit or turnover. The guidance also suggests that the group auditor "will wish" to directly perform (or related auditors to directly perform) the work on the financial information of components that are of individual financial significance and components that may include significant risks of material misstatement in the financial statements.

Whilst we recognize that a group auditor might consider the risk too high of accepting an engagement at which his audit of the components represents less than 50% value of the financial statements, we feel that setting a standard amount: "approximately 50%", is not robust enough to support the sentiment in Paragraphs 11 and 13 that reflect on the importance of the group auditor being involved in the audit of components that are of individual financial significance, or the group auditor's consideration of significant risks of material misstatement.

We therefore propose that the first sentence in Paragraph 12 is amended as follows: "It will be unusual for a group auditor to accept an engagement to audit group financial statements where the ~~group auditor and related auditors directly perform work on less than approximately 50%~~ other auditors directly perform work on the majority of the group assets.....". This will allow the group auditor to use own judgement as to what the majority means, which includes application of his own firm's risk policies and procedures.

\*\*\*\*\*

\*