

**ASA 550**  
(October 2009)

# Explanatory Statement

## *ASA 550 Related Parties*

Issued by the **Auditing and Assurance Standards Board**

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**Australian Government**

**Auditing and Assurance Standards Board**

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This Explanatory Statement is available on the Auditing and Assurance Standards Board (AUASB) website: [www.auasb.gov.au](http://www.auasb.gov.au)

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## **Reasons for Issuing Auditing Standard ASA 550 *Related Parties***

The Auditing and Assurance Standards Board (AUASB) issues Auditing Standard ASA 550 *Related Parties* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is as an independent statutory board of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001* (the Act), the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the International Auditing and Assurance Standards Board (IAASB) for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards. The IAASB has undertaken a programme to redraft, and in some cases, revise, in “clarity” format, the entire suite of ISAs. Accordingly, the AUASB has decided to revise and redraft the Australian Auditing Standards using the equivalent redrafted ISAs.

## **Operative Date**

ASA 550 *Related Parties* is operative for financial reporting periods commencing on or after 1 January 2010.

## **Purpose of Auditing Standard ASA 550 *Related Parties***

The purpose of the Auditing Standard is to establish Requirements and to provide Application and Other Explanatory Material to auditors regarding their responsibilities relating to related party relationships and transactions in an audit of a financial report.

## Explanatory Statement ASA 550 *Related Parties*

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### Main Features

The Auditing Standard:

- (a) requires the auditor to gain an understanding of related party relationships and transactions and to obtain information relevant to identifying the risks of material misstatement associated with related party relationships and transactions;
- (b) describes risk assessment procedures and responses to assessed risks;
- (c) requires the auditor to evaluate the accounting and disclosure of related party relationships and transactions;
- (d) when relevant, requires the auditor to obtain written representations; and
- (e) requires the auditor to communicate significant matters to those charged with governance.

### Preamble and Overall Objectives

ASA 550 is to be read in conjunction with ASA 101 *Preamble to Australian Auditing Standards*, which sets out the intentions of the AUASB on how the Australian Auditing Standards, operative for financial reporting periods commencing on or after 1 January 2010, are to be understood, interpreted and applied. ASA 550 is to be read also in conjunction with ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.

### Process of making Australian Auditing Standards

The AUASB's Strategic Direction, *inter alia*, provides that the AUASB develop Australian Auditing Standards that:

- have a clear public interest focus and are of the highest quality;
- use the International Standards on Auditing (ISAs) of the International Auditing and Assurance Standards Board (IAASB) as the underlying standards;
- conform with the Australian regulatory environment; and
- are capable of enforcement.

## **Explanatory Statement ASA 550 *Related Parties***

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In implementing the FRC's Strategic Direction, the AUASB has undertaken a process of revision and redrafting of the Australian Auditing Standards that has:

- updated the form, layout and content of the Australian Auditing Standards;
- addressed the legal enforceability of mandatory obligations;
- maintained clarity of the auditor's obligations;
- incorporated appropriate references to Australian laws and regulations;
- clearly identified, by use of the prefix "Aus", AUASB additions to paragraphs in the Requirements or the Application and Other Explanatory Material; and
- included other amendments as necessary.

### **Consultation Process prior to issuing the Auditing Standard**

The AUASB has consulted publicly as part of its due process in developing the Auditing Standard. Exposure Draft ED 20/08 *Proposed Auditing Standard: Related Parties* (Re-issuance of ASA 550), was issued on 10 November 2008 with a 30 day comment period.

As an integral part of its consultation with the public, the AUASB sought comments on specific questions including:

- the completeness and accuracy of references in the Auditing Standard to relevant laws and regulations;
- the significant costs, if any, and benefits, of compliance with any additional Requirements under the Auditing Standard; and
- whether or not there exist any matters of public interest affecting the issuance of the Auditing Standard.

Submissions were received by the AUASB and these were considered as part of the development and finalisation of the Auditing Standard.

## Regulation Impact Statement

A Regulation Impact Statement (RIS) has been prepared in connection with the redrafting of Australian Auditing Standards in Clarity format, including *ASA 550 Related Parties*.

The RIS has considered both the expected benefits and expected costs of the introduction of clarified auditing standards, including comments provided by stakeholders during the redrafting process. It concluded that expected benefits to users of audit services, users of audit reports, auditors and the Australian economy in general are, on balance, likely to outweigh expected costs.

## Main Differences from *ASA 550 Related Parties* (April 2006)

The main differences between the Auditing Standard and the Auditing Standard that it supersedes, *ASA 550 Related Parties* (April 2006), are:

1. Auditing Standard ASA 550 is written in the 'clarity' format using the equivalent International Standard on Auditing (*ISA 550 Related Parties*) as the underlying Auditing Standard. Consequently, the format, layout, and paragraph numbering styles are different from the extant Auditing Standard.
2. In accordance with normal updating practice, ASA 550 (using *ISA 550* as the underlying standard) has been subject to a major revision in addition to redrafting in "clarity" format. In ASA 550, the Requirements and Application and Other Explanatory Material paragraphs are either:
  - (a) new paragraphs;
  - (b) elevations of extant guidance paragraphs; or
  - (c) rewording of extant paragraphs.
3. The following Requirements included in Auditing Standard ASA 550 are in part, or full, the main additional Requirements to the extant Auditing Standard:
  - (a) "The engagement team discussion that ASA 315 and ASA 240 require shall include specific consideration of the susceptibility of the financial report to material misstatement due to fraud or error that could result from the

## Explanatory Statement ASA 550 *Related Parties*

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entity's related party relationships and transactions.”  
(Ref: Para 12)

- (b) “The auditor shall share relevant information obtained about the entity's related parties with the other members of the engagement team.” (Ref: Para 17)
- (c) “If the auditor identifies fraud risk factors (including circumstances relating to the existence of a related party with dominant influence) when performing the risk assessment procedures and related activities in connection with related parties, the auditor shall consider such information when identifying and assessing the risks of material misstatement due to fraud in accordance with ASA 240.” (Ref: Para 19)
- (d) “If the auditor identifies related parties or significant related party transactions that management has not previously identified or disclosed to the auditor, the auditor shall:
  - Promptly communicate the relevant information to the other members of the engagement team;
  - Where the applicable financial reporting framework establishes related party requirements:
    - Request management to identify all transactions with the newly identified related parties for the auditor's further evaluation; and
    - Enquire as to why the entity's controls over related party relationships and transactions failed to enable the identification or disclosure of the related party relationships or transactions;
  - Perform appropriate substantive audit procedures relating to such newly identified related parties or significant related party transactions;
  - Reconsider the risk that other related parties or significant related party transactions may exist that management has not previously identified or disclosed to the auditor, and perform additional audit procedures as necessary; and

## Explanatory Statement ASA 550 *Related Parties*

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- If the non-disclosure by management appears intentional (and therefore indicative of a risk of material misstatement due to fraud), evaluate the implications for the audit.” (Ref: Para 22)
  - (e) “For identified significant related party transactions outside the entity’s normal course of business, the auditor shall:
    - Inspect the underlying contracts or agreements, if any, and evaluate whether:
      - The business rationale (or lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets;
      - The terms of the transactions are consistent with management’s explanations; and
      - The transactions have been appropriately accounted for and disclosed in accordance with the applicable financial reporting framework.” (Ref: Para 23)
  - (f) “If management has made an assertion in the financial report to the effect that a related party transaction was conducted on terms equivalent to those prevailing in an arm’s length transaction, the auditor shall obtain sufficient appropriate audit evidence about the assertion.” (Ref: Para 24)
  - (g) “The auditor shall include in the audit documentation the names of the identified related parties and the nature of the related party relationships.” (Ref: Para 28)
4. Significant Application and Other Explanatory Material, linked to the additional Requirements listed at 3. above, is also included in the Auditing Standard.