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Basis for Conclusions ***ASA 600 Special Considerations—Audits of a Group Financial Report (Including the Work of Component Auditors)***

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



Australian Government

Auditing and Assurance Standards Board

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**Basis for Conclusions ASA 600 *Special Considerations—Audits of a Group Financial Report*
(Including the Work of Component Auditors)**

Basis for Conclusions ASA 600 *Special Considerations—Audits of a Group Financial Report* (Including the Work of Component Auditors) has been developed by the Auditing and Assurance Standards Board (AUASB) to provide a background to, and rationale for the development and approval of the Standard by the AUASB. The Basis for Conclusions relates to, but does not form part of, ASA 600.

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BASIS FOR CONCLUSIONS

ASA 600 *Special Considerations—Audits of a Group Financial Report (Including the Work of Component Auditors)*

This Basis for Conclusions is issued by the Auditing and Assurance Standards Board (AUASB). It provides a background to, and rationale for the development and approval of the Standard by the AUASB. The Basis of Conclusions relates to, but does not form part of, *ASA 600 Special Considerations—Audits of a Group Financial Report (Including the Work of Component Auditors)*, and is not a substitute for reading the Standard.

Background

1. In accordance with its mandates under section 227 of the *Australian Securities and Investments Commission Act 2001* and the Financial Reporting Council's Strategic Direction, the AUASB's policy is to adopt the International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB), unless there is a compelling reason not to do so. In addition, the AUASB is required to make such amendments to the ISAs to ensure the Australian Auditing Standards both exhibit and conform to the Australian regulatory environment and statutory requirements. Further amendments are made where there are compelling reasons to do so and are made with a public interest focus. Refer paragraphs 11-12 of this Basis of Conclusions document for further detail on compelling reason amendments.
2. The IAASB issued *ISA 600 Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)* in April 2022.
3. In December 2016, the IAASB approved a combined project proposal to address the revision of ISQC 1¹, ISA 220² and ISA 600³. The project proposal combined the topics of quality control and group audits due to the interaction of the issues affecting these standards, while the timing of the projects considered the degree of interaction between the various projects of the IAASB.
4. The IAASB's objective in revising ISA 600 was to strengthen the auditor's approach to planning and performing a group audit and clarify the interaction of ISA 600 to the other ISAs.
5. The IAASB released an exposure draft of proposed ISA 600 in April 2020 and in June 2020 the AUASB exposed the IAASB exposure draft to gather feedback from Australian stakeholders to inform its submission to the IAASB.
6. The AUASB sought input from stakeholders in three principal ways. The first was from hosting a series of virtual roundtable meeting with stakeholders representing assurance providers from medium and large audit firms, the public sector and the professional accounting bodies across Australia; the second was through an open invitation to provide comments placed on the AUASB website; and the third was by way of formal discussions between AUASB members.
7. Based on the feedback received, the AUASB provided a submission to the IAASB in October 2020. Refer to the [AUASB's full submission](#).

¹ ISQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagement*.

² ISA 220 *Quality Control for an Audit of Financial Statements*.

³ ISA 600 *Special Considerations—Audits of Group Financial Statements*.

8. The AUASB monitored the development of ISA 600 to ensure that the issues included in the submission to the IAASB were appropriately addressed. Further details regarding the development of ISA 600 and how the IAASB addressed feedback on their exposure draft can be found in the [ISA 600 Basis for Conclusions](#) on the IAASB’s website.

Scope

9. This Basis for Conclusions applies to *ASA 600 Special Considerations—Audits of a Group Financial Report (Including the Work of Component Auditors)*.

Major Issues raised by Respondents on Exposure

10. The AUASB received feedback from respondents on the Australian exposure of ISA 600 with the major issues included in the submission to the IAASB relating to:
- (a) The scope and application of the proposed standard;
 - (b) The role and importance of component auditors;
 - (c) Access considerations particularly considering equity accounted investments; and
 - (d) Strengthening documentation requirements.

The AUASB included these issues in its submission to the IAASB. Appendix 1 details all major feedback received from Australian stakeholders included in the AUASB’s submission to the IAASB and how those matters have been addressed in the final ISA 600.

Compelling reasons assessment

11. The adoption of international standards and any changes to adopted standards are governed by the AUASB’s [AUASB Policy and Process for International Conformance and Harmonisation of Standards](#) (Harmonisation Policy). The policies and procedures incorporate “compelling reasons” tests which must be used to support changes to the international standards. Changes are made only when the AUASB is satisfied that there are persuasive reasons to do so. Further to paragraph 1 of this Basis of Conclusions document, compelling reasons fall broadly into two categories: legal and regulatory; and principles and practices considered appropriate having regard to the public interest in Australia.
12. The AUASB has made the following compelling reason amendments upon adoption of ISA 600 in Australia as ASA 600:
- (a) Joint auditors are not arrangements that are allowable in Australia and accordingly, the AUASB has deleted application material paragraph A25. The AUASB considers that the Compelling Reason test is triggered under Australian regulatory arrangements. The deletion will ensure effective and efficient compliance with the regulatory framework in Australia and will not result in a requirement that is lesser than or in conflict with the international standard.
 - (b) Carried forward (slightly amended) from extant ASA 600 is an application material paragraph Aus A34.1, that reminds auditors of the *Corporations Act 2001* requirement for the officer or auditor of a controlled entity to give the principal auditor access to the controlled entity’s books; and give the auditor any information, explanation or assistance required under section 323A of the Act. The AUASB considers that the Compelling Reason test is triggered under Australian regulatory arrangements. The insertion will ensure effective and efficient compliance with the regulatory framework in Australia and will not result in a requirement that is lesser than or in conflict with the international standard.

- (c) In relation to Appendix 1 to ASA 600, the illustrative Auditor’s Report, the AUASB has deleted the International example and has replaced with a *Corporations Act 2001* example. The reason for the change is to be consistent with example reports provided under ASA 700 *Forming an Opinion and Reporting on a Financial Report* and within extant ASA 600. The Australian example report is in the public interest as it aids in consistency in application of the standards.

Conclusion

- 13. The AUASB voted to approve and issue ASA 600 and the conforming and consequential amendments on 13 May 2022.
- 14. In reaching its conclusions the AUASB considered:
 - (a) all stakeholder feedback;
 - (b) the IAASB’s due process and consideration as to whether ISA 600 should be re-exposed;
 - (c) whether the amendments made to the standard by the IAASB since exposure were in response to submissions from stakeholders on the exposure draft, have not changed the fundamental approach and principles on which the standard is based, and did not require the re-expose of the standard.

* * *

Appendix 1

How more significant issues raised in the AUASB submission to the IAASB have been addressed in the final ISA 600

Scope and Applicability	<i>How addressed in the standard</i>
<p><i>Extracts from AUASB submission to IAASB</i></p> <p>The AUASB generally supported the scope and applicability of ED ISA 600, including the definition of group financial statements and the linkage to a consolidation process. However, the AUASB recommended that the scope and application of the standard be clarified and that the introductory paragraphs be strengthened in this regard. The AUASB recommended the following enhancements to the introductory paragraphs:</p> <ul style="list-style-type: none"> • The definition of “group financial statements” could be further enhanced by directly incorporating the “consolidation process” definition which is a key element to the entry point into the standard. • ED ISA 600 scopes in some very simple group structures for example a single entity with branches for which no component auditors are used. While the AUASB understands that the underlying ISAs are applicable and ED ISA 600 is special considerations only, there is expected to be an extensive amount of documentation to effectively demonstrate that the special considerations of ED ISA 600 are largely not applicable. The AUASB recommends that for single entity structures, the auditor exercises professional judgement in determining whether ED ISA 600 applies. The IAASB could determine the factors to be considered in exercising professional judgement including considerations such as inherent risk factors, commonality of controls and centralisation of activities. 	<ul style="list-style-type: none"> • Entry point into the standard clear and upfront in the introduction, including a point to emphasises that the term ‘consolidation process’ isn’t only the financial reporting concept of such a process; • Description of consolidation process included in the definition of group financial statements; • Clarification that branches or divisions are within the scope of ISA 600 (same as extant) including for simple structures. Recognising in application material that not all the requirements of the standard may be applicable in simple structures for example requirements related to component auditors may not be applicable. The AUASB suggestion that professional judgment may be appropriate for these simple structures was considered by the Taskforce but rejected on the basis that the exercise of professional judgement in this situation would be contrary to the desire of respondents for ‘brighter lines’ and exercise of professional judgement here could lead to inconsistent application in practice; • Upfront reference to ISA 220 to provide greater clarity that ISA 600 may be applied where appropriate when the auditor involves other auditors in the audit of financial reports that are not group financial reports (similar to extant ISA 600 and already facilitated in paragraph A1 of Revised ISA 220).

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<ul style="list-style-type: none"> • The title of ED ISA 600 refers to ‘group financial statements’, with there being a common understanding of the use of the term ‘group’ and ‘consolidation process’, there is a risk that practitioners do not realise that they are working with a group engagement under ISA 600. To aid in the clarity of the applicability of ED ISA 600, the AUASB recommends that the introductory section of the proposed standard should specifically call out that ED ISA 600 includes such single entities in certain circumstances. • Extant ISA 600 applies, as appropriate, when the auditor involves other auditors in the audit of financial reports that are not group financial reports. For example, an auditor may involve another auditor to observe the inventory count or inspect physical fixed assets at a remote location. Recently approved ISA 220 <i>Quality Management for an Audit of Financial Statements</i> (ISA 220 Revised), application material paragraph A1 indicates that this may still be the case under the recently approved new standards. The AUASB recommends that the introductory section to ED ISA 600 demonstrates this link to ISA 220 Revised as this linkage is not currently clear. 	
<p>Risk Based Approach</p> <p><i>Extracts from AUASB submission to IAASB</i></p> <p>While the AUASB strongly supported a risk-based approach to ISA 600, the AUASB raised the following substantive issues in relation to risk-based approach:</p> <ul style="list-style-type: none"> • While the AUASB largely supports that the decision of the nature and extent of the involvement of component auditors should be determined by the group engagement team based on an assessment of risk, the AUASB highlights that component auditors may not hold a sense of accountability and responsibility towards the group auditor and that this may 	<p><i>How addressed in the standard</i></p> <ul style="list-style-type: none"> • The introductory section links the use of component auditors to ISA 220 which 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 group scenario these resources include Component Auditors. ASA 600 recognises upfront the importance of component auditors in that they may have greater experience 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. However, the Group Engagement Partner remains

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<p>impact on the auditors exercise of professional scepticism in the audit work assigned to them.</p> <ul style="list-style-type: none"> • The standard may diminish the importance and role of component auditors, with too great a focus on the group auditor. The AUASB noted that ED ISA 600 does not sufficiently recognise that, for groups that are complex and large that may need localised knowledge and specialisation, high levels of involvement by component auditors is of critical importance to audit quality. • In responding to the assessed risk of material misstatement, the group engagement team may decide to use one or multiple approaches to gather audit evidence. When the group engagement team uses component auditors, the engagement team may request the component auditor to design and perform further audit procedures on the entire financial information of the component. The AUASB considers that the meaning of ‘Design and perform further audit procedures on the entire financial information of the component’ is not sufficiently clear. The AUASB recommends that the IAASB clarify whether this approach is meant to be a full-scope reasonable assurance engagement. 	<p>ultimately responsible for managing and achieving quality on the group audit engagement.</p> <ul style="list-style-type: none"> • Established a framework for planning and performing a group audit engagement. The framework emphasises special considerations for establishing the overall group audit strategy and group audit plan and highlights the importance of involving component auditors throughout all phases of a group audit. The associated application material includes: <ul style="list-style-type: none"> ○ matters that may influence the groups determination of components at which work needs to be performed, ○ factors that may influence the group auditor’s determination on whether to involve component auditors (consideration of resources needed). Having these factors and highlighting the importance of having component auditors involved, helps in addressing concerns raised by respondents about the strong focus on the group auditor’s responsibility and a top-down approach to the group audit that may undermine the important role of the component auditor. • Focuses the group auditor’s attention on identifying, assessing and responding to the risks of material misstatement of the group financial statements, and emphasises the importance of designing and performing procedures that are appropriate to respond to those assessed risks of material misstatement. For the three approaches for assigning further audit procedures to component auditors (e.g., design and perform further audit procedures on the entire financial information of the component, design and perform further audit procedures on one or more classes of transactions, account balances or disclosures or perform specific further audit procedures): <ul style="list-style-type: none"> ○ For each approach, a description as to when the approach could be used to assign procedures to component auditors.
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	<ul style="list-style-type: none"> ○ Examples added for each approach to further clarify when the approach could be used to assign further procedures to component auditors.
<p>Access</p> <p>The AUASB acknowledges and supports the inclusion of enhancements to the requirements and application within ED ISA 600 in relation to access to people and information. We note however that some of the requirements and application material appear to only identify and acknowledge existing practical challenges rather than provide group engagement teams with appropriate guidance on how to overcome such restrictions. For example, the requirements and application guidance do not outline how the group engagement team is expected to apply sufficient and appropriate risk assessment procedures if the group includes equity accounted investments, where there are restrictions on access to information and people.</p>	<p><i>How addressed in the standard</i></p> <ul style="list-style-type: none"> • Clarifies how to address restrictions on access to audit documentation, people and information in a group audit, including restrictions on access to component management, those charged with governance of the component, component auditors, or information at the components. • Access considerations for equity accounting investments are explicitly addressed in the application material.
<p>Materiality</p> <p>The AUASB supported the focus in ED ISA 600 on component materiality, however, raised the following matters for consideration:</p> <ul style="list-style-type: none"> • Paragraph 29 of ED-600 states that component materiality “shall be lower than group performance materiality”. The AUASB suggests that this is changed to “Shall not be greater than group performance materiality”. When a group has a component that represents almost 100% of the group, it may be reasonable to use the group performance materiality to audit this component. • While the AUASB supports the factors to consider in determining component performance materiality, Australian 	<p><i>How addressed in the standard</i></p> <ul style="list-style-type: none"> • Clarification that proposed ISA 600 does not require component performance materiality to be established for each class of transactions, account balance or disclosure at the component level • Application material describing that there are circumstances in which 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. • Definition of aggregation risk to be included in ISA 320 through a conforming amendment. • Additional application material on situations in which a collaborative approach between the group auditor and a component auditor may be

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<p>stakeholders have raised concern with the lack of guidance and examples regarding the actual calculation and allocation of performance materiality. The AUASB encourages the IAASB to provide implementation guidance and examples of performance materiality outside of the revised standard.</p> <ul style="list-style-type: none"> Paragraph A13 of ISA 320 refers to aggregation risk without a clear definition of aggregation risk within ISA 320. While the AUASB supports the definition of aggregation risk as included at paragraph 9(a) of ED ISA 600, the AUASB queries the placement of this definition. The AUASB recommends that aggregation risk is defined within ISA 320 with the special considerations of such risk being addressed in ISA 600. 	<p>appropriate in determining component performance materiality, and to emphasise the importance of two-way communication, particularly if the number and magnitude of misstatements identified by the component auditor are higher than expected.</p> <ul style="list-style-type: none"> Worked examples of determining component performance materiality will be provided outside of proposed ISA 600, consistent with previous Board discussions. Examples, may have unintended consequences, including perceptions of the IAASB sanctioning a particular or ‘best’ approach
<p>Documentation</p> <p><i>Extracts from AUASB submission to IAASB</i></p> <p>The AUASB considered that the documentation requirements could be strengthened if it is explicitly tied into the requirements with respect to the overall assessment of sufficiency and appropriateness of audit evidence</p>	<p><i>How addressed in the standard</i></p> <p>Expanded and enhanced requirements and application material including:</p> <ul style="list-style-type: none"> Stronger link between the documentation requirements and the group auditor’s overall evaluation of the sufficiency and appropriateness of audit evidence obtained on which to base the group audit opinion Reinforce the general principle that the audit documentation for a group audit consists of the documentation in the group auditor’s file together with the component auditor documentation, and that the component auditor documentation generally resides in the component auditor’s audit file and need not be replicated in the group auditor’s audit file Specific requirements and application material when component auditors are involved including: <ul style="list-style-type: none"> Basis for group auditor’s determination of the competence and capabilities of component auditors Documentation of the direction and supervision of component auditors and the review of their work

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	<ul style="list-style-type: none">○ Strengthening the requirements relating review of component auditor’s workpapers○ Additional considerations when access to component auditor documentation is restricted
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