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Via e-mail – EDComments@ifac.org

Germany, Stuttgart, March 31, 2004

Exposure Draft: ISA 600 (Revised), „The Work of Related Auditors and Other Auditors in the Audit of Group Financial Statements“ incl. IAPS, “The Audit of Group Financial Statements”

Dear Mr. Sylph:

The German Certified Public Accountants Society e.V. (the “GCPAS” which is the professional organization of US-Certified Public Accountants in Germany) would like to thank you for the opportunity to provide the International Auditing and Assurance Standards Board (IAASB) with our comments on the Exposure Draft of the Proposed International Standard on Auditing (ISA) 600 “The Work of Related Auditors and Other Auditors in the Audit of Group Financial Statements” (hereinafter referred to as “the proposed standard”) and on the Proposed International Auditing Practice Statement (IAPS), “The Audit of Group Financial Statements”.

The GCPAS believes that – due to recent developments in the audit and assurance area (such as the Parmalat case) – it is helpful and necessary to give more and adjusted guidance on how work of either Related Auditors or Other Auditors shall be integrated in the audit of Group Financial Statements.

In this comment letter, we will address general comments of broader application first before commenting on matters specific to individual paragraphs of the proposed standard.

General Comments

We fully support the concept in the proposed standard that the “**Sole Responsibility**” should be the preferred method. The Group Auditor should be (under consideration of his professional judgment) solely responsible in the determination of the scope of work to be performed either directly or by a Related Auditor or Other Auditor respectively (see paragraph 10).

However, this does not exclude the possibility to use the audit evidence obtained by the Related Auditor or Other Auditor in connection with the statutory audit – if required to express an audit opinion on a component’s financial statements – as appropriately stated in paragraph 14.

We also fully support the concept in paragraph 5 of the proposed standard that in case the Group Auditor takes the “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. Such a reference could – instead of providing more transparency of the audit process – possibly lead the addressees of the auditor’s report to believe that a kind of “**Division of Responsibility**” exists and could, therefore, increase the already existing expectation gap. The exception to this strict rule in paragraph 31, however, is not only acceptable but strongly required since the full liable Group Auditor should have the possibility to explain the reasons and circumstances of a scope limitation which is due to the work of the Other Auditor or Related Auditor not providing sufficient audit evidence or due to insufficient access to information as stated in paragraph 19 and 20.

Consequently, we support the new concept stated in paragraph 6 in connection with paragraph 7 (f) and (h) of the proposed standard that the “Division of Responsibility” does not apply in case of a Related Auditor but only in case of an Other Auditor. This distinction between Other Auditors and Related Auditors – in comparison to ISA 600 currently in force – will reduce the scope of applying the “Division of Responsibility”.

Although we understand the matter of the IAASB that – due to practical implementation issues – the “Division of Responsibility” should be retained as an alternative approach, we do not fully agree with granting the auditor with the possibility to voluntarily select one of the methods. The wording of the standard should clearly state that the “Division of Responsibility” should only be accepted in exceptional cases where some or all of the additional requirements for “Sole Responsibility” cannot be fulfilled. We would anticipate that due to such a changed wording the acceptance of “Sole Responsibility” will increase. We believe that all relevant stakeholders on the capital markets will accept – if not in short term – at least in mid term the “Sole Responsibility” as best practice if not as only acceptable approach for audits of group financial statements.

We are aware of the possible impact on national standards or national law and regulations in IFAC member states where “Division of Responsibility” is permitted. The emerging pressure on such standards and regulations can help to reach the main intention of the IAASB: To promote consistent practices by auditors worldwide, here to be considered as the “Sole Responsibility”.

We furthermore agree with the idea of **not** implementing any requirement that a certain percentage of work must be performed directly by the Group Auditor. In implementing such a regulation the professional judgment of the Group Auditor would be limited. Applying the “Sole Responsibility” the Group Auditor is fully liable for the whole Group Audit even if he used the work of Other Auditors or Related Auditors in accordance with the revised ISA 600. The full liability of the Group Auditor can be considered as appropriate and possibly as the best practice approach and regulator to ensure a high quality audit of the whole group financial statements.

In addition, we believe that a regulation requiring a certain percentage of work to be performed by the Group Auditor would lead to even more concentration on the auditing and assurance market and, consequently, would weaken the situation for mid-tier accounting firms or independent networks acting as Related Auditors. Nevertheless, the threshold mentioned in IAPS (paragraph 12) that it will be unusual to accept an engagement to audit group financial statements where Group Auditors and Related Auditors directly perform work on less than approximately 50% of certain criteria, does not contradict our aforementioned statement since the possibility to involve Related Auditors has been included.

To implement only the concept of “Sole Responsibility” would be also in line with the

Proposal for a Directive of the European Parliament and of the Council on statutory audit of annual accounts and consolidated accounts and amending Council Directives 78/660/EEC and 83/349/EEC/ COM/2004/0177 final - COD 2004/0065 */*

(for full text please see:

http://www.europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexapi!prod!CELEXnumdoc&lg=EN&numdoc=52004PC0177&model=guichett)

Article 27 (a) of the aforementioned proposal for a directive states clearly that only the concept of “Sole Responsibility” will be allowed in the European Union if the directive will be adopted as proposed. The European Commission states clearly that the Parmalat case is the reason for this decision.

In paragraph 22 of the proposed standard the Group Auditor will be enforced to obtain written communications on the work performed on the component’s financial statements by the Related Auditor or Other Auditor. Furthermore, the standard lists some requirements for such written communications [paragraph 22 (a)-(e)]. In order to achieve a structured and uniformed presentation of such written communications, we would propose to implement on an international level the so called “**Long Form Auditor’s Report**” which is in Germany – in addition to the “**Short Form Auditor’s Report**” – required by law (Sec. 321 German Commercial Code – *Prüfungsbericht*) and in detail described in the German National Auditing Standard IDW PS 450 *Grundsätze ordnungsmäßiger Berichterstattung bei Abschlussprüfungen* [Generally Accepted Standards for the Long Form Auditor’s Report] issued by the IFAC member organization IDW – Institut der Wirtschaftsprüfer in Deutschland e.V. (www.idw.de). In this case, the Related Auditor or Other Auditor could provide the solely responsible Group Auditor with the “Long Form Auditor’s Report”. The detailed information included in the “Long Form Auditor’s Report” would enhance the ability of the Group Auditor to apply his professional judgment on how to consider the work of the Related Auditor or Other Auditor. The German “Long Form Auditor’s Report” is much more detailed and structured than the so called “Auditor’s Opinion on Reporting Packages” widely used and individually designed in content and length in the international audit practice. Implementing a “Long Form Auditor’s Report” – such as the German one – on an international level (preferable by issuing a new respective ISA) would, therefore, enhance the current reporting procedures and promote consistent practices by auditors worldwide.

Comments on Specific Paragraphs

Paragraph 22 (e):

According to paragraph 22 (e) of the proposed standard the Group Auditor should receive a list identifying “uncorrected misstatements” of the components financial statements. The list, however, does not include those items regarded to be “clearly inconsequential misstatements”.

We believe that the second sentence in this paragraph 22 (e) should be **deleted**. The Group Auditor should be provided with all information and evidence incurred during the audit of all components. Only under those circumstances he could determine with his own professional judgment whether the group financial statements are presented fairly in all material respects.

By eliminating the second sentence, possible conflict areas (i.e. the determination of “inconsequential” misstatements) are reduced. Furthermore, only the Group Auditor can determine at group level whether in total all “inconsequential” misstatements are still immaterial from a group perspective.

Instead, we would recommend to add the following sentence to paragraph 22 (e) in order to clarify the meaning of “uncorrected misstatements”:

“Uncorrected misstatements” include all adjusting journal entries with effect on the income statement as well as all mere reclassifying journal entries (either with effect on the balance sheet or on the income statement) which were identified by the auditor during the audit but not recorded in the financial statements of the respective component.

At least, we believe that the term “clearly inconsequential misstatements” as stated in paragraph 22 (e) needs to be defined in order to avoid that the Related Auditor or the Other Auditor can independently decide whether to report certain misstatements to the Group Auditor or not. The concept of materiality correctly considers, that the sum of many “clearly inconsequential misstatements” can be (e.g. aggregated with uncorrected immaterial misstatements of other component’s financial information as stated in paragraph 33) material to the group financial statements. The Group Auditor, therefore, should be provided with all identified misstatements in order to apply his professional judgment on the level of the group financial statements.

We believe that the wording in paragraph 22 (e) in connection with paragraph 33 of the proposed standard are for example not consistent with the wording in paragraph 6 of ISA 320 *Audit Materiality*. The distinction between “clearly inconsequential misstatements” (paragraph 22 (e) of the proposed standard) and “relatively small amounts” (paragraph 6 ISA 320) is not defined in the proposed standard. Hence, we see the risk that the application of both standards will not be consistent.

In addition, paragraph 31 of the proposed IAPS states that the group auditor also communicates a threshold below which misstatements are regarded as clearly inconsequential and, as a result, need not be communicated to the Group Auditor, does not resolve the aforementioned problem: The sum of inconsequential misstatements can exceed the defined threshold and the Group Auditor should be informed accordingly.



Paragraph 38:

The last sentence of paragraph 38 states in case of “Division of Responsibility” the following:

“When there is more than one other auditor, the percentages covered by the other auditors may be stated in the aggregate.”

We would recommend to **delete** the aforementioned sentence since we believe that the fact whether the responsibility is divided with more than one other auditor and to which extent each of the other auditors is involved in the audit of the group financial statements is certainly a useful and necessary information for the addressees of the auditors report on the group financial statements.

Thank you for the opportunity to comment on this Exposure Draft. If you have any questions regarding the comments in this letter, please contact us at kontakt@gcpas.de. We would be pleased to discuss this letter with you or another member of the IAASB staff.

Respectfully submitted,

GCPAS International Standards on Auditing Practice Committee (ISAPC)

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