



441 G St. N.W.  
Washington, DC 20548

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Mr. Willie Botha  
Technical Director  
International Auditing and Assurance Standards Board  
529 Fifth Avenue  
New York, NY 10017

**GAO's Response to the International Auditing and Assurance Standards Board's Exposure Draft Proposed Part 10, *Audits of Group Financial Statements of the Proposed International Standards of Auditing for Audits of Financial Statements of Less Complex Entities***

This letter provides GAO's comments on the International Auditing and Assurance Standards Board's (IAASB) Proposed Part 10, *Audits of Group Financial Statements of the Proposed International Standards of Auditing for Audits of Financial Statements of Less Complex Entities*. GAO promulgates generally accepted government auditing standards, which provide professional standards for auditors of government entities in the United States.

We do not support the IAASB's efforts to make group audit part of a standard for the audit of financial statements of less complex entities (LCE). We believe that group audit is inherently complex and not appropriate for LCE financial statement audit. We believe that there is an inherent risk of group audit for LCEs being applied to more complex entities. In addition, we find that the qualitative characteristics are insufficient to identify appropriate circumstances for using a group audit for an LCE financial statement audit. While we agree with the exclusion of component auditors in group audits of LCEs, we find that the exclusion of requirements and application material for how to use component auditors in the limited circumstances allowed problematic.

The IAASB seeks comment on three specific questions. Our responses to the questions follow in the enclosure to this letter.

Thank you for the opportunity to comment. If you have questions about this letter or would like to discuss any of our responses, please feel free to contact me at (202) 512-3133 or [dalkinj@gao.gov](mailto:dalkinj@gao.gov).

A handwritten signature in black ink, appearing to read "James R. Dalkin".

James R. Dalkin  
Director  
Financial Management and Assurance

Enclosure

## Enclosure

### ***Responses to Questions to the International Auditing and Assurance Standards Board's Proposed Audits of Group Financial Statements of the Proposed International Standards on Auditing for Audits of Financial Statements of Less Complex Entities***

- 1. In the Authority, do you agree with the proposed prohibition on the use of the proposed International Standards on Auditing (ISA) for Less Complex Entities (LCE) for group audits where component auditors are involved, other than in limited circumstances where physical presence is required?**

We do not believe that group audit should be included in the ISA for LCE as a group audit is inherently complex. We believe that there is an inherent risk of group audit for LCEs being applied to more complex entities, which may lead to inappropriate conclusions.

The decision to exclude component auditors is misleading. The allowance for component auditors to be used in limited circumstances, for example physical presence being required, creates the risk for application more broadly and outside of the intention of the ISA. In addition, if component auditors are allowed to be used in a limited capacity, then the standard should have guidance for how a component auditor should be treated, which can be achieved by adding such guidance to the ISA for LCEs or adding language directing auditors to other ISAs for guidance.

- 2. In the Authority, do you agree with the proposed group-specific qualitative characteristics to describe the scope of group audits for which the proposed ISA for LCE is designed to be used?**

We do not believe that group audit for LCE is appropriate, but we analyzed the qualitative characteristics to assess whether, if implemented, the characteristics would be sufficient as presented. We do not believe that the identified group-specific qualitative characteristics are sufficient to describe a consistent appropriate scope of group audits for which the proposed ISA for LCEs is designed to be used.

We find the first characteristic related to group structure and activities arbitrary and unable to ensure that the group is not complex. This concern is not alleviated with the consideration of the other group-specific qualitative characteristics or the general characteristics for an LCE.

We suggest modifying the characteristic to better describe the nature and size of entities that could be part of the group and the number of jurisdictions in which the entities are located. This should include an understanding that the group structure and activities include an appropriate mix of number of entities and jurisdictions and not a separate consideration of them.

In addition, we do not believe that the consolidation process description as a characteristic is sufficient in its definition as simple is not adequate to clarify what level, structure, detail, size, or number of consolidations are appropriate for a group audit under the ISA for LCEs. We find that the use of examples helps but without more description of an appropriate level of consolidation, the examples may be interpreted as the accepted consolidations.

**3. Do you agree with the content of proposed Part 10 and related conforming amendments?**

We do not agree with including part 10 in the proposed ISA for LCEs, as group audit by its nature is a type of engagement that is not less complex. The structure of part 10 demonstrates in multiple places that complexity exists in group audits, even as identified for a LCE group audit. For example, the risk of material misstatement due to fraud has increased complexity because of the need to consider members of the group in the evaluation. In addition, the consolidation process in part 10 does not convey that the consolidation should be simple or basic and shows that it is instead a complicating factor in the audit.

Also, while component auditors are to be included only in limited circumstances, there is no discussion in part 10 of the appropriate application or consideration of a component auditor. We believe that if use of component auditors is allowed, in any way, then part 10 should include a section discussing their use.