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American Institute of Accountants. Committee on Auditing Procedure

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## *Using the Work and Reports of Other Auditors*

(Supersedes Paragraphs 32 to 36 of Chapter 10  
of *Statement on Auditing Procedure No. 33*)

1. The purpose of this Statement is to establish guidelines for reporting on financial statements when the independent auditor (referred to herein as the principal auditor) utilizes the work and reports of other independent auditors who have examined the financial statements of one or more subsidiaries, divisions, branches, or other components included in the financial statements presented.

### **Principal Auditor's Course of Action**

2. The auditor in this situation may have performed all but a relatively minor portion of the work, or significant parts of the examination may have been performed by other auditors. In the latter case he must decide whether his own participation is sufficient to enable him to serve as the principal auditor and to report

*Issued by the Committee on Auditing Procedure  
American Institute of Certified Public Accountants*

as such on the financial statements. In deciding this question, the auditor should consider, among other things, the materiality of the portion of the financial statements he has examined in comparison with the portion examined by other auditors, the extent of his knowledge of the overall financial statements and the importance of the components he examined in relation to the enterprise as a whole.

3. If the auditor decides that it is appropriate for him to serve as the principal auditor, he must then decide whether to make reference in his report<sup>1</sup> to the examination made by another auditor. If the principal auditor decides to assume responsibility for the work of the other auditor insofar as that work relates to the principal auditor's expression of an opinion on the financial statements taken as a whole, no reference should be made to the other auditor's examination. On the other hand, if the principal auditor decides not to assume that responsibility, his report should make reference to the examination of the other auditor and should indicate clearly the division of responsibility between himself and the other auditor in expressing his opinion on the financial statements. Regardless of the principal auditor's decision, the other auditor remains responsible for the performance of his own work and for his own report.

#### **Decision Not to Make Reference**

4. If the principal auditor is able to satisfy himself as to the independence and professional reputation of the other auditor (see paragraph 10), and takes steps he considers appropriate to satisfy himself as to the other auditor's examination (see paragraph 12), he may be able to express an opinion on the financial statements taken as a whole without making reference in his report to the examination of the other auditor. If the principal auditor decides to take this position, he should not state in his report that part of the examination was made by another auditor because to do so may cause a reader to misinterpret the degree of responsibility being assumed.

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<sup>1</sup> See paragraph 9 for example of appropriate reporting when reference is made to the examination of other auditors.

5. Ordinarily, the principal auditor would be able to adopt this position when:
- a. Part of the examination is made by another independent auditor which is an associated or correspondent firm and whose work is acceptable to the principal auditor based on his knowledge of the professional standards and competence of that firm; or
  - b. The other auditor was retained by the principal auditor and the work was performed under the principal auditor's guidance and control; or
  - c. The principal auditor, whether or not he selected the other auditor, nevertheless takes steps he considers necessary to satisfy himself as to the other auditor's examination and accordingly is satisfied as to the reasonableness of the accounts for the purpose of inclusion in the financial statements on which he is expressing his opinion; or
  - d. The portion of the financial statements examined by the other auditor is not material to the financial statements covered by the principal auditor's opinion.

#### **Decision to Make Reference**

6. On the other hand, the principal auditor may decide to make reference to the examination of the other auditor when he expresses his opinion on the financial statements. In some situations, it may be impracticable for the principal auditor to review the other auditor's work or to use other procedures which in the judgment of the principal auditor would be necessary for him to satisfy himself as to the other auditor's examination. Also, if the financial statements of a component examined by another auditor are material in relation to the total, the principal auditor may decide, regardless of any other considerations, to make reference in his report to the examination of the other auditor.

7. When the principal auditor decides that he will make reference to the examination of the other auditor, his report should indicate clearly, in both the scope and opinion paragraphs, the

division of responsibility as between that portion of the financial statements covered by his own examination and that covered by the examination of the other auditor. The report should disclose the magnitude of the portion of the financial statements examined by the other auditor. This may be done by stating the dollar amounts or percentages of one or more of the following: total assets, total revenues or other appropriate criteria, whichever most clearly reveals the portion of the financial statements examined by the other auditor. The other auditor may be named, but only with his express permission and provided his report is presented together with that of the principal auditor.<sup>2</sup>

8. Reference in the report of the principal auditor to the fact that part of the examination was made by another auditor is not to be construed as a qualification of the opinion but rather as an indication of the divided responsibility between the auditors who conducted the examinations of various components of the overall financial statements.<sup>3</sup>

9. An example of appropriate reporting by the principal auditor indicating the division of responsibility when he makes reference to the examination of the other auditor follows:

We have examined the consolidated balance sheet of X Company and subsidiaries as of December 31, 197— and the related consolidated statements of income and retained earnings and of changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We did not examine the financial statements of B Company, a consolidated subsidiary,

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<sup>2</sup> As to filings with the Securities and Exchange Commission, Rule 2-05 of Regulation S-X states: "If, with respect to the certification of the financial statements of any person, the principal accountant relies on an examination made by another independent public accountant of certain of the accounts of such person or its subsidiaries, the certificate of such other accountant shall be filed . . . ; however, the certificate of such other accountant need not be filed (a) if no reference is made directly or indirectly to such other accountant's examination in the principal accountant's certificate, or (b) if, having referred to such other accountant's examination, the principal accountant states in his certificate that he assumes responsibility for such other accountant's examination in the same manner as if it had been made by him."

<sup>3</sup> See also paragraph 11, Chapter 10 of *Statement on Auditing Procedure No. 33*.

which statements reflect total assets and revenues constituting 20% and 22%, respectively, of the related consolidated totals. These statements were examined by other auditors whose report thereon has been furnished to us and our opinion expressed herein, insofar as it relates to the amounts included for B Company, is based solely upon the report of the other auditors.

In our opinion, based upon our examination and the report of other auditors, the accompanying consolidated balance sheet and consolidated statements of income and retained earnings and of changes in financial position present fairly. . . .

When two or more auditors in addition to the principal auditor participate in the examination, the percentages covered by the other auditors may be stated in the aggregate.

### **Procedures Applicable to Both Methods of Reporting**

10. Whether or not the principal auditor decides to make reference to the examination of the other auditor, he should make inquiries concerning the professional reputation and independence of the other auditor. He also should adopt appropriate measures to assure the coordination of his activities with those of the other auditor in order to achieve a proper review of matters affecting the consolidating or combining of accounts in the financial statements. These inquiries and other measures may include procedures such as the following:

- a. Make inquiries as to the professional reputation and standing of the other auditor to one or more of the following:
  - (i) The American Institute of Certified Public Accountants, the applicable state society of Certified Public Accountants and/or the local chapter, or in the case of a foreign auditor, his corresponding professional organization.
  - (ii) Other practitioners.
  - (iii) Bankers and other credit grantors.
  - (iv) Other appropriate sources.

- b. Obtain a representation from the other auditor that he is independent under the requirements of the American Institute of Certified Public Accountants and, if appropriate, the requirements of the Securities and Exchange Commission.
- c. Ascertain through communication with the other auditor:
  - (i) That he is aware that the financial statements of the component which he is to examine are to be included in the financial statements on which the principal auditor will report and that the other auditor's report thereon will be relied upon (and, where applicable, referred to) by the principal auditor.
  - (ii) That he is familiar with accounting principles generally accepted in the United States and with the generally accepted auditing standards promulgated by the American Institute of Certified Public Accountants and will conduct his examination and will report in accordance therewith.
  - (iii) That he has knowledge of the relevant financial reporting requirements for statements and schedules to be filed with regulatory agencies such as the Securities and Exchange Commission, if appropriate.
  - (iv) That a review will be made of matters affecting elimination of intercompany transactions and accounts and, if appropriate in the circumstances, the uniformity of accounting practices among the components included in the financial statements.

(Inquiries as to matters under a, and c (ii) and (iii) ordinarily would be unnecessary if the principal auditor already knows the professional reputation and standing of the other auditor and if the other auditor's primary place of practice is in the United States.)

11. If the results of inquiries and procedures by the principal auditor with respect to matters described in paragraph 10 lead

him to the conclusion that he can neither assume responsibility for the work of the other auditor insofar as that work relates to the principal auditor's expression of an opinion on the financial statements taken as a whole, nor report in the manner set forth in paragraph 9, he should appropriately qualify his opinion or disclaim an opinion on the financial statements taken as a whole. His reasons therefor should be stated, and the magnitude of the portion of the financial statements to which his qualification extends should be disclosed.

**Additional Procedures Under Decision  
Not to Make Reference**

12. When the principal auditor decides not to make reference to the examination of the other auditor, in addition to satisfying himself as to the matters described in paragraph 10, he should also consider whether to perform one or more of the following procedures:

- a. Visit the other auditor and discuss the audit procedures followed and results thereof.
- b. Review the audit programs of the other auditor. In some cases, it may be appropriate to issue instructions to the other auditor as to the scope of his audit work.
- c. Review the working papers of the other auditor, including his evaluation of internal control and his conclusions as to other significant aspects of the engagement.

13. In some circumstances the principal auditor may consider it appropriate to participate in discussions regarding the accounts with management personnel of the component whose financial statements are being examined by other auditors and/or to make supplemental tests of such accounts. The determination of the extent of additional procedures, if any, to be applied rests with the principal auditor alone in the exercise of his professional judgment and in no way constitutes a reflection on the adequacy of the other auditor's work. Because the principal auditor in this case assumes responsibility for his opinion on the financial statements on which he is reporting without making reference to the other auditor's examination, his judgment must govern as to the extent of procedures to be undertaken.

**Qualifications in Other Auditor's Report**

14. If the opinion of the other auditor is qualified, the principal auditor should decide whether the subject of the qualification is of such nature and significance in relation to the financial statements on which the principal auditor is reporting that it would require qualification of his own report. If the subject of the qualification is not material in relation to such financial statements and the other auditor's report is not presented, the principal auditor need not make reference in his report to the qualification; if the other auditor's report is presented, the principal auditor may wish to make reference to such qualification and its disposition.

**Restated Financial Statements of Prior Years Following a Pooling of Interests**

15. Following a pooling of interests transaction, an auditor may be asked to report on restated financial statements for one or more prior years when other auditors have examined one or more of the entities included in such financial statements. In some of these situations the auditor may decide that he has not examined a sufficient portion of the financial statements for such prior year or years to enable him to serve as principal auditor (see paragraph 2). Also, in such cases, it often is not possible or it may not be appropriate or necessary for the auditor to satisfy himself with respect to the restated financial statements. In these circumstances, it may be appropriate for him to express his opinion solely with respect to the compilation of such statements; however, no opinion should be expressed unless the auditor has examined the statements of at least one of the entities included in the restatement for at least the latest period presented. The following is an illustration of appropriate reporting on compilation which can be presented in an additional paragraph of the auditor's report following the standard scope and opinion paragraphs covering the consolidated financial statements for the current year:

We previously examined and reported upon the consolidated statements of income and of changes in financial

position of XYZ Company for the year ended December 31, 19\_\_\_\_ prior to its restatement for 19\_\_\_\_ poolings of interests. The contribution of XYZ Company to revenues and net income represented \_\_\_\_% and \_\_\_\_% of the respective restated totals. Separate financial statements of the pooled companies included in the 19\_\_\_\_ restated consolidated statement of income were examined and reported upon separately by other auditors. We also have reviewed, as to compilation only, the accompanying consolidated statements of income and of changes in financial position for the year ended December 31, 19\_\_\_\_ after restatement for 19\_\_\_\_ poolings of interests; in our opinion, such consolidated statements have been properly compiled on the basis described in Note X of notes to consolidated financial statements.

16. In reporting on the compilation of restated financial statements as described in the preceding paragraph, the auditor does not assume responsibility for the work of other auditors nor the responsibility for expressing an opinion on the restated financial statements taken as a whole. His review is directed toward procedures which will enable him to express an opinion as to proper compilation only. These procedures include checking the compilation for mathematical accuracy and for conformity of the compilation methods with generally accepted accounting principles. For example, the auditor should review and make inquiries regarding such matters as the following:

- a. Elimination of intercompany transactions and accounts.
- b. Combining adjustments and reclassifications.
- c. Adjustments to treat like items in a comparable manner, if appropriate.
- d. The manner and extent of presentation of disclosure matters in the restated financial statements and notes thereto.

The auditor should also consider the application of procedures contained in paragraph 10.

### Predecessor Auditor

17. When one auditor succeeds another, the successor auditor must establish the basis for expressing his opinion on the financial statements for the first year he examines and on the consistency of the application of accounting principles in that year as compared with the preceding year. This may be done by applying appropriate auditing procedures to the account balances at the beginning of the period under examination. The scope of this work may be reduced by consultation with the predecessor auditor and review of the predecessor auditor's working papers. In such cases, it is customary for the predecessor auditor, as a matter of professional courtesy, to make himself available to the successor auditor for consultation and to make his working papers available for review. However, in reporting on his examination, the successor auditor should not make reference to the report or work of the predecessor auditor as the basis in part for his own opinion.<sup>4</sup> If the successor auditor is unable to obtain satisfaction as to the opening balances insofar as they affect the financial statements for the period on which he is reporting, he should appropriately qualify his opinion or disclaim an opinion and state his reasons for doing so.

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<sup>4</sup> This is not intended to preclude the auditor from stating that the financial statements for the prior year were examined by other auditors when those statements are presented for comparison purposes. See paragraph 48, Chapter 10 of *Statement on Auditing Procedure No. 33*.

*The Statement entitled "Using the Work and Reports of Other Auditors" was adopted unanimously by the twenty-one members of the Committee on Auditing Procedure.*

### NOTE

*Statements on Auditing Procedure present the considered opinion of the Committee on Auditing Procedure, which is the senior technical committee of the Institute designated to issue pronouncements on auditing matters. Departures from the Committee's recommendations must be justified by those who do not follow them.*

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