ISSAI Guidelines on Financial Audit-1
The Supreme Audit Institution of Bangladesh has always been striving to keep itself abreast of what is happening in modern auditing. INTOSAI, the global platform of the Auditors General issues guidelines and standards which work as benchmarks for conducting government audit across the nations. After extensive research and hard work put together by member nations, INTOSAI published International Standards of Supreme Audit Institutions, commonly known as ISSAI in 2010.

To meet country specific requirements, SAI Bangladesh has its own audit codes and standards. The ‘Audit Code’, ‘Government Auditing Standards’ and ‘Code of Ethics for Government Auditors’ were published as per the best international practices prevailing at the time of issue. The ISSAI came into audit domain later on. So, Audit Codes and Standards need to be updated in line with ISSAI. The SAI Bangladesh is working in that direction.

Through the project, titled “Strengthening Public Expenditure Management Program”(SPEMP-B) a good number of ISSAI-based financial, compliance and performance audits had been conducted on pilot basis. The audit reports were highly appreciated by the executives and other stakeholders. These audits were administered by respective audit directorates with active cooperation from national and international consultants of SPEMP-B.

The ISSAI-based audits have shown performance excellence which need to be mainstreamed in the Audit Directorates. Formal instructions have been issued to audit directorates to replicates ISSAI-based audit done under the said project. ISSAI-based Audit Manuals are also being finalized which, if made available in handy form to the auditors, would enable them to conduct field audit smoothly and skillfully.

The present compilation of ISSAI is issued as “Financial Audit Guidelines-1” to be followed by Bengali translation. During application of the ISSAI if any error or omission is noticed, the matter may please be intimated to the Office of the Comptroller and Auditor General of Bangladesh.

Masud Ahmed  
Comptroller and Auditor General of Bangladesh  
Dated, Dhaka 3.11.2015
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The International Standards of Supreme Audit Institutions, ISSAI, are issued by the International Organization of Supreme Audit Institutions, INTOSAI. For more information visit www.issai.org
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INTRODUCTION

1. Professional standards and guidelines are essential for the credibility, quality and professionalism of public sector auditing. The International Standards of Supreme Audit Institutions (ISSAIs) developed by the International Organisation of Supreme Audit Institutions (INTOSAI) aim to promote independent and effective auditing by supreme audit institutions (SAIs).

2. The ISSAIs encompass public sector auditing requirements at the organisational (SAI) level, while on the level of individual audits they aim to support the members of INTOSAI in the development of their own professional approach in accordance with their mandates and with national laws and regulations.

3. INTOSAI’s Framework of Professional Standards has four levels. Level 1 contains the framework’s founding principles. Level 2 (ISSAIs 10-99) sets out prerequisites for the proper functioning and professional conduct of SAIs in terms of organisational considerations that include independence, transparency and accountability, ethics and quality control, which are relevant for all SAI audits. Levels 3 and 4 address the conduct of individual audits and include generally recognised professional principles that underpin the effective and independent auditing of public sector entities.

4. The Fundamental Auditing Principles at level 3 (ISSAIs 100-999) draw and elaborate on ISSAI 1 – The Lima Declaration and the ISSAIs at level 2 and provide an authoritative international frame of reference defining public sector auditing.

5. Level 4 translates the Fundamental Auditing Principles into more specific and detailed operational guidelines that can be used on a daily basis in the conduct of an audit and as auditing standards when national auditing standards have not been developed. This level comprises General Auditing Guidelines (ISSAIs 1000-4999) which set the requirements for financial, performance and compliance auditing.

6. ISSAI 100 – Fundamental Principles of Public sector Auditing provides detailed information on:
   - the purpose and authority of the ISSAIs;
   - the framework for public sector auditing;
   - the elements of public sector auditing;
   - the principles to be applied in public sector auditing.
PURPOSE AND AUTHORITY OF THE ISSAI

7. ISSAI 100 establishes fundamental principles which are applicable to all public sector audit engagements, irrespective of their form or context. ISSAIs 200, 300 and 400 build on and further develop the principles to be applied in the context of financial, performance and compliance auditing respectively. They should be applied in conjunction with the principles set out in ISSAI 100. The principles in no way override national laws, regulations or mandates or prevent SAIs from carrying out investigations, reviews or other engagements which are not specifically covered by the existing ISSAIs.

8. The Fundamental Auditing Principles form the core of the General Auditing Guidelines at level 4 of the ISSAI framework. The principles can be used to establish authoritative standards in three ways:

- as a basis on which SAIs can develop standards;
- as a basis for the adoption of consistent national standards;
- as a basis for adoption of the General Auditing Guidelines as standards.

SAIs may choose to compile a single standard setting document, a series of such documents or a combination of standard setting and other authoritative documents.

SAIs should declare which standards they apply when conducting audits, and this declaration should be accessible to users of the SAI’s reports. Where the standards are based on several sources taken together, this should also be stated. SAIs are encouraged to make such declarations part of their audit reports; however, a more general form of communication may be used.

9. An SAI may declare that the standards it has developed or adopted are based on or are consistent with the Fundamental Auditing Principles only if the standards fully comply with all relevant principles.

Audit reports may include a reference to the fact that the standards used were based on or consistent with the ISSAI or ISSAIs relevant to the audit work carried out. Such reference may be made by stating:
We conducted our audit in accordance with [standards], which are based on [or consistent with] the Fundamental Auditing Principles (ISSAIs 100-999) of the International Standards of Supreme Audit Institutions.

In order to properly adopt or develop auditing standards based on the Fundamental Auditing Principles, an understanding of the entire text of the principles is necessary. To achieve this, it may be helpful to consult the relevant guidance in the General Auditing Guidelines.

10. SAIs may choose to adopt the General Auditing Guidelines as their authoritative standards. In such cases the auditor must comply with all ISSAIs relevant to the audit. Reference to the ISSAIs applied may be made by stating:

... We conducted our audit[s] in accordance with the International Standards of Supreme Audit Institutions.

In order to enhance transparency, the statement may further specify which ISSAI or range of ISSAIs the auditor has considered relevant and applied. This may be done by adding the following phrase:

The audit[s] was [were] based on ISSAI[s] xxx [number and name of the ISSAI or range of ISSAIs].

11. The International Standards on Auditing (ISAs) issued by the International Federation of Accountants (IFAC) are incorporated into the financial audit guidelines (ISSAIs 1000-2999). In financial audits reference may therefore be made either to the ISSAIs or to the ISAs. The ISSAIs provide additional public sector guidance ('Practice Notes'), but the requirements of the auditor in financial audits are the same. The ISAs constitute an indivisible set of standards and the ISSAIs in which they are incorporated may not be referred to individually. If the ISSAIs or the ISAs have been adopted as the SAI’s standards for financial audits, the auditor’s report should include a reference to those standards. This applies equally to financial audits conducted in combination with other types of audit.

12. Audits may be conducted in accordance with both the General Auditing
Guidelines and standards from other sources provided that no contradictions arise. In such cases reference should be made both to such standards and to the ISSAI.

FRAMEmWORK FOR PUBLIC SECTOR AUDITING

Mandate

13. An SAI will exercise its public sector audit function within a specific constitutional arrangement and by virtue of its office and mandate, which ensure sufficient independence and power of discretion in performing its duties. The mandate of an SAI may define its general responsibilities in the field of public sector auditing and provide further prescriptions concerning the audits and other engagements to be performed.

14. SAIs may be mandated to perform many types of engagements on any subject of relevance to the responsibilities of management and those charged with governance and the appropriate use of public funds and assets. The extent or form of these engagements and the reporting thereon will vary according to the legislated mandate of the SAI concerned.

15. In certain countries, the SAI is a court, composed of judges, with authority over State accountants and other public officials who must render account to it. There exists an important relationship between this jurisdictional authority and the characteristics of public sector auditing. The jurisdictional function requires the SAI to ensure that whoever is charged with dealing with public funds is held accountable and, in this regard, is subject to its jurisdiction.

16. An SAI may make strategic decisions in order to respond to the requirements in its mandate and other legislative requirements. Such decisions may include which auditing standards are applicable, which engagements will be conducted and how they will be prioritised.

Public sector auditing and its objectives

17. The public sector audit environment is that in which governments and other public sector entities exercise responsibility for the use of resources derived from taxation and other sources in the delivery of services to citizens and other recipients. These entities are accountable for their management and performance, and for the use of resources, both to those that provide the resources and to those,
including citizens, who depend on the services delivered using those resources. Public sector auditing helps to create suitable conditions and reinforce the expectation that public sector entities and public servants will perform their functions effectively, efficiently, ethically and in accordance with the applicable laws and regulations.

18. In general public sector auditing can be described as a systematic process of objectively obtaining and evaluating evidence to determine whether information or actual conditions conform to established criteria. Public sector auditing is essential in that it provides legislative and oversight bodies, those charged with governance and the general public with information and independent and objective assessments concerning the stewardship and performance of government policies, programmes or operations.

19. SAIs serve this aim as important pillars of their national democratic systems and governance mechanisms and play an important role in enhancing public sector administration by emphasising the principles of transparency, accountability, governance and performance. ISSAI 20 – *Principles of Transparency and Accountability* contain guidance in this regard.

20. All public sector audits start from objectives, which may differ depending on the type of audit being conducted. However, all public sector auditing contributes to good governance by:

- providing the intended users with independent, objective and reliable information, conclusions or opinions based on sufficient and appropriate evidence relating to public entities;
- enhancing accountability and transparency, encouraging continuous improvement and sustained confidence in the appropriate use of public funds and assets and the performance of public administration;
- reinforcing the effectiveness of those bodies within the constitutional arrangement that exercise general monitoring and corrective functions over government, and those responsible for the management of publicly-funded activities;
- creating incentives for change by providing knowledge, comprehensive analysis and well-founded recommendations for improvement.
21. In general, public sector audits can be categorised into one or more of three main types: audits of financial statements, audits of compliance with authorities and performance audits. The objectives of any given audit will determine which standards apply.

**Types of public sector audit**

22. The three main types of public sector audit are defined as follows:

- **Financial audit** focuses on determining whether an entity’s financial information is presented in accordance with the applicable financial reporting and regulatory framework. This is accomplished by obtaining sufficient and appropriate audit evidence to enable the auditor to express an opinion as to whether the financial information is free from material misstatement due to fraud or error.

- **Performance audit** focuses on whether interventions, programmes and institutions are performing in accordance with the principles of economy, efficiency and effectiveness and whether there is room for improvement. Performance is examined against suitable criteria, and the causes of deviations from those criteria or other problems are analysed. The aim is to answer key audit questions and to provide recommendations for improvement.

- **Compliance audit** focuses on whether a particular subject matter is in compliance with authorities identified as criteria. Compliance auditing is performed by assessing whether activities, financial transactions and information are, in all material respects, in compliance with the authorities which govern the audited entity. These authorities may include rules, laws and regulations, budgetary resolutions, policy, established codes, agreed terms or the general principles governing sound public sector financial management and the conduct of public officials.

23. SAIs may carry out audits or other engagements on any subject of relevance to the responsibilities of management and those charged with governance and the appropriate use of public resources. These engagements may include reporting on the quantitative outputs and outcomes of the entity’s service delivery activities, sustainability reports, future resource requirements, adherence to
internal control standards, real-time audits of projects or other matters. SAIs may also conduct combined audits incorporating financial, performance and/or compliance aspects.

ELEMENTS OF PUBLIC SECTOR AUDITING

24. Public sector auditing is indispensable for the public administration, as the management of public resources is a matter of trust. Responsibility for the management of public resources in line with intended purposes is entrusted to an entity or person who acts on behalf of the public. Public sector auditing enhances the confidence of the intended users by providing information and independent and objective assessments concerning deviations from accepted standards or principles of good governance.

All public sector audits have the same basic elements: the auditor, the responsible party, intended users (the three parties to the audit), criteria for assessing the subject matter and the resulting subject matter information. They can be categorised as two different types of audit engagement: attestation engagements and direct reporting engagements.

The three parties

25. Public sector audits involve at least three separate parties: the auditor, a responsible party and intended users. The relationship between the parties should be viewed within the context of the specific constitutional arrangements for each type of audit.

- **The auditor**: In public sector auditing the role of auditor is fulfilled by the Head of the SAI and by persons to whom the task of conducting the audits is delegated. The overall responsibility for public sector auditing remains as defined by the SAI’s mandate.

- **The responsible party**: In public sector auditing the relevant responsibilities are determined by constitutional or legislative arrangement. The responsible parties may be responsible for the subject matter information, for managing the subject matter or for addressing recommendations, and may be individuals or organisations.

- **Intended users**: The individuals, organisations or classes thereof for
whom the auditor prepares the audit report. The intended users may be legislative or oversight bodies, those charged with governance or the general public.

Subject matter, criteria and subject matter information

26. Subject matter refers to the information, condition or activity that is measured or evaluated against certain criteria. It can take many forms and have different characteristics depending on the audit objective. An appropriate subject matter is identifiable and capable of consistent evaluation or measurement against the criteria, such that it can be subjected to procedures for gathering sufficient and appropriate audit evidence to support the audit opinion or conclusion.

27. The criteria are the benchmarks used to evaluate the subject matter. Each audit should have criteria suitable to the circumstances of that audit. In determining the suitability of criteria the auditor considers their relevance and understandability for the intended users, as well as their completeness, reliability and objectivity (neutrality, general acceptance and comparability with the criteria used in similar audits). The criteria used may depend on a range of factors, including the objectives and the type of audit. Criteria can be specific or more general, and may be drawn from various sources, including laws, regulations, standards, sound principles and best practices. They should be made available to the intended users to enable them to understand how the subject matter has been evaluated or measured.

28. Subject matter information refers to the outcome of evaluating or measuring the subject matter against the criteria. It can take many forms and have different characteristics depending on the audit objective and audit scope.

Types of engagement

29. There are two types of engagement:

- In **attestation engagements** the responsible party measures the subject matter against the criteria and presents the subject matter information, on which the auditor then gathers sufficient and appropriate audit evidence to provide a reasonable basis for expressing a conclusion.

- In **direct reporting engagements** it is the auditor who measures or evaluates the subject matter against the criteria. The auditor selects the
subject matter and criteria, taking into consideration risk and materiality. The outcome of measuring the subject matter against the criteria is presented in the audit report in the form of findings, conclusions, recommendations or an opinion. The audit of the subject matter may also provide new information, analyses or insights.

30. Financial audits are always attestation engagements, as they are based on financial information presented by the responsible party. Performance audits are normally direct reporting engagements. Compliance audits may be attestation or direct reporting engagements, or both at once. The following constitute the subject matter or the subject matter information in the three types of audit covered by the ISSAIs:

- **Financial audit**: The subject matter of a financial audit is the financial position, performance, cash flow or other elements which are recognised, measured and presented in financial statements. The subject matter information is the financial statements.

- **Performance audit**: The subject matter of a performance audit is defined by the audit objectives and audit questions. The subject matter may be specific programmes, entities or funds or certain activities (with their outputs, outcomes and impacts), existing situations (including causes and consequences) as well as non-financial or financial information about any of these elements. The auditor measures or evaluates the subject matter to assess the extent to which the established criteria have or have not been met.

- **Compliance audit**: The subject matter of a compliance audit is defined by the scope of the audit. It may be activities, financial transactions or information. For attestation engagements on compliance it is more relevant to focus on the subject matter information, which may be a statement of compliance in accordance with an established and standardised reporting framework.
Confidence and assurance in public sector auditing

The need for confidence and assurance

31. The intended users will wish to be confident about the reliability and relevance of the information which they use as the basis for taking decisions. Audits therefore provide information based on sufficient and appropriate evidence, and auditors should perform procedures to reduce or manage the risk of reaching inappropriate conclusions. The level of assurance that can be provided to the intended user should be communicated in a transparent way. Due to inherent limitations, however, audits can never provide absolute assurance.

Forms of providing assurance

32. Depending on the audit and the users’ needs, assurance can be communicated in two ways:
   - Through opinions and conclusions which explicitly convey the level of assurance. This applies to all attestation engagements and certain direct reporting engagements.
   - In other forms. In some direct reporting engagements the auditor does not give an explicit statement of assurance on the subject matter. In such cases the auditor provides the users with the necessary degree of confidence by explicitly explaining how findings, criteria and conclusions were developed in a balanced and reasoned manner, and why the combinations of findings and criteria result in a certain overall conclusion or recommendation.

Levels of assurance

33. Assurance can be either reasonable or limited.

   Reasonable assurance is high but not absolute. The audit conclusion is expressed positively, conveying that, in the auditor's opinion, the subject matter is or is not compliant in all material respects, or, where relevant, that the subject matter information provides a true and fair view, in accordance with the applicable criteria.

   When providing limited assurance, the audit conclusion states that, based on the procedures performed, nothing has come to the auditor’s attention to cause the
auditor to believe that the subject matter is not in compliance with the applicable criteria. The procedures performed in a limited assurance audit are limited compared with what is necessary to obtain reasonable assurance, but the level of assurance is expected, in the auditor's professional judgment, to be meaningful to the intended users. A limited assurance report conveys the limited nature of the assurance provided.

**PRINCIPLES OF PUBLIC SECTOR AUDITING**

34. The principles detailed below are fundamental to the conduct of an audit. Auditing is a cumulative and iterative process. However, for the purposes of presentation the fundamental principles are grouped by principles related to the SAI’s organisational requirements, general principles that the auditor should consider prior to commencement and at more than one point during the audit and principles related to specific steps in the audit process.

**Areas covered by the principles for public sector auditing**

**GENERAL PRINCIPLES**

- Ethics & independence
- Professional judgment, due care and skepticism
- Quality control
- Audit team management & skills
- Audit risk
- Materiality
- Documentation
- Communication

**PRINCIPLES RELATED TO THE AUDIT PROCESS**

1. **Planning the audit**
   - Establish the terms of the audit
   - Obtain understanding
   - Conduct risk assessment or problem analysis
   - Identify risks of fraud
   - Develop an audit plan

2. **Conducting the audit**
   - Perform the planned audit procedures to obtain audit evidence
   - Evaluate audit evidence and draw conclusions

3. **Reporting and follow-up**
   - Prepare a report based on the conclusions reached
   - Follow up on reported matters as relevant
Organisational requirements

35. **SAIs should establish and maintain appropriate procedures for ethics and quality control**

Each SAI should establish and maintain procedures for ethics and quality control on an organisational level that will provide it with reasonable assurance that the SAI and its personnel are complying with professional standards and the applicable ethical, legal and regulatory requirements. *ISSAI 30 – Code of Ethics and ISSAI 40 – Quality Control for SAIs* contain guidance in this regard. The existence of these procedures at SAI level is a prerequisite for applying or developing national standards based on the Fundamental Auditing Principles.

**General principles**

**Ethics and independence**

36. **Auditors should comply with the relevant ethical requirements and be independent**

Ethical principles should be embodied in an auditor’s professional behaviour. The SAIs should have policies addressing ethical requirements and emphasising the need for compliance by each auditor. Auditors should remain independent so that their reports will be impartial and be seen as such by the intended users.

Auditors can find guidance on independence in the *ISSAI 10 – Mexico Declaration on SAI Independence*. Guidance on the key ethical principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour are defined in *ISSAI 30 – Code of Ethics*.

**Professional judgment, due care and skepticism**

37. **Auditors should maintain appropriate professional behaviour by applying professional skepticism, professional judgment and due care throughout the audit**

The auditor’s attitude should be characterised by professional skepticism and professional judgment, which are to be applied when forming decisions about the appropriate course of action. Auditors should exercise due care to ensure that their professional behaviour is appropriate.
Professional skepticism means maintaining professional distance and an alert and questioning attitude when assessing the sufficiency and appropriateness of evidence obtained throughout the audit. It also entails remaining open-minded and receptive to all views and arguments.

Professional judgment implies the application of collective knowledge, skills and experience to the audit process. Due care means that the auditor should plan and conduct audits in a diligent manner. Auditors should avoid any conduct that might discredit their work.

**Quality control**

38. **Auditors should perform the audit in accordance with professional standards on quality control**

An SAI’s quality control policies and procedures should comply with professional standards, the aim being to ensure that audits are conducted at a consistently high level. Quality control procedures should cover matters such as the direction, review and supervision of the audit process and the need for consultation in order to reach decisions on difficult or contentious matters. Auditors can find additional guidance in *ISSAI 40 – Quality Control for SAIs*.

**Audit team management and skills**

39. **Auditors should possess or have access to the necessary skills**

The individuals in the audit team should collectively possess the knowledge, skills and expertise necessary to successfully complete the audit. This includes an understanding and practical experience of the type of audit being conducted, familiarity with the applicable standards and legislation, an understanding of the entity’s operations and the ability and experience to exercise professional judgment. Common to all audits is the need to recruit personnel with suitable qualifications, offer staff development and training, prepare manuals and other written guidance and instructions concerning the conduct of audits, and assign sufficient audit resources. Auditors should maintain their professional competence through ongoing professional development.

Where relevant or necessary, and in line with the SAI’s mandate and the applicable legislation, the auditor may use the work of internal auditors, other auditors or experts. The auditor’s procedures should provide a sufficient basis for
using the work of others, and in all cases the auditor should obtain evidence of other auditors’ or experts’ competence and independence and the quality of the work performed. However, the SAI has sole responsibility for any audit opinion or report it might produce on the subject matter; that responsibility is not reduced by its use of work done by other parties.

The objectives of internal audit are different from those of external audit. However, both internal and external audit promote good governance through contributions to transparency and accountability for the use of public resources, as well as economy, efficiency and effectiveness in public administration. This offers opportunities for coordination and cooperation and the possibility of eliminating duplication of effort.

Some SAIs use the work of other auditors at state, provincial, regional, district or local level, or of public accounting firms that have completed audit work related to the audit objective. Arrangements should be made to ensure that any such work was carried out in accordance with public sector auditing standards.

Audits may require specialised techniques, methods or skills from disciplines not available within the SAI. In such cases experts may be used to provide knowledge or carry out specific tasks or for other purposes.

**Audit risk**

40. **Auditors should manage the risks of providing a report that is inappropriate in the circumstances of the audit**

The audit risk is the risk that the audit report may be inappropriate. The auditor performs procedures to reduce or manage the risk of reaching inappropriate conclusions, recognising that the limitations inherent to all audits mean that an audit can never provide absolute certainty of the condition of the subject matter. When the objective is to provide reasonable assurance, the auditor should reduce audit risk to an acceptably low level given the circumstances of the audit. The audit may also aim to provide limited assurance, in which case the acceptable risk that criteria are not complied with is greater than in a reasonable assurance audit. A limited assurance audit provides a level of assurance that, in the auditor’s professional judgment, will be meaningful to the intended users.
Materiality

41. Auditors should consider materiality throughout the audit process

Materiality is relevant in all audits. A matter can be judged material if knowledge of it would be likely to influence the decisions of the intended users. Determining materiality is a matter of professional judgment and depends on the auditor’s interpretation of the users’ needs. This judgment may relate to an individual item or to a group of items taken together. Materiality is often considered in terms of value, but it also has other quantitative as well as qualitative aspects. The inherent characteristics of an item or group of items may render a matter material by its very nature. A matter may also be material because of the context in which it occurs.

Materiality considerations affect decisions concerning the nature, timing and extent of audit procedures and the evaluation of audit results. Considerations may include stakeholder concerns, public interest, regulatory requirements and consequences for society.

Documentation

42. Auditors should prepare audit documentation that is sufficiently detailed to provide a clear understanding of the work performed, evidence obtained and conclusions reached

Audit documentation should include an audit strategy and audit plan. It should record the procedures performed and evidence obtained and support the communicated results of the audit. Documentation should be sufficiently detailed to enable an experienced auditor, with no prior knowledge of the audit, to understand the nature, timing, scope and results of the procedures performed, the evidence obtained in support of the audit conclusions and recommendations, the reasoning behind all significant matters that required the exercise of professional judgment, and the related conclusions.

Communication

43. Auditors should establish effective communication throughout the audit process

It is essential that the audited entity be kept informed of all matters relating to the
audit. This is key to developing a constructive working relationship. Communication should include obtaining information relevant to the audit and providing management and those charged with governance with timely observations and findings throughout the engagement. The auditor may also have a responsibility to communicate audit-related matters to other stakeholders, such as legislative and oversight bodies.

**Principles related to the audit process**

**Planning an audit**

44. **Auditors should ensure that the terms of the audit have been clearly established**

Audits may be required by statute, requested by a legislative or oversight body, initiated by the SAI or carried out by simple agreement with the audited entity. In all cases the auditor, the audited entity’s management, those charged with governance and others as applicable should reach a common formal understanding of the terms of the audit and their respective roles and responsibilities. Important information may include the subject, scope and objectives of the audit, access to data, the report that will result from the audit, the audit process, contact persons, and the roles and responsibilities of the different parties to the engagement.

45. **Auditors should obtain an understanding of the nature of the entity/programme to be audited**

This includes understanding the relevant objectives, operations, regulatory environment, internal controls, financial and other systems and business processes, and researching the potential sources of audit evidence. Knowledge can be obtained from regular interaction with management, those charged with governance and other relevant stakeholders. This may mean consulting experts and examining documents (including earlier studies and other sources) in order to gain a broad understanding of the subject matter to be audited and its context.

46. **Auditors should conduct a risk assessment or problem analysis and revise this as necessary in response to the audit findings**

The nature of the risks identified will vary according to the audit objective. The
Auditor should consider and assess the risk of different types of deficiencies, deviations or misstatements that may occur in relation to the subject matter. Both general and specific risks should be considered. This can be achieved through procedures that serve to obtain an understanding of the entity or programme and its environment, including the relevant internal controls. The auditor should assess the management’s response to identified risks, including its implementation and design of internal controls to address them. In a problem analysis the auditor should consider actual indications of problems or deviations from what should be or is expected. This process involves examining various problem indicators in order to define the audit objectives. The identification of risks and their impact on the audit should be considered throughout the audit process.

47. Auditors should identify and assess the risks of fraud relevant to the audit objectives
Auditors should make enquiries and perform procedures to identify and respond to the risks of fraud relevant to the audit objectives. They should maintain an attitude of professional skepticism and be alert to the possibility of fraud throughout the audit process.

48. Auditors should plan their work to ensure that the audit is conducted in an effective and efficient manner
Planning for a specific audit includes strategic and operational aspects. Strategically, planning should define the audit scope, objectives and approach. The objectives refer to what the audit is intended to accomplish. The scope relates to the subject matter and the criteria which the auditors will use to assess and report on the subject matter, and is directly related to the objectives. The approach will describe the nature and extent of the procedures to be used for gathering audit evidence. The audit should be planned to reduce audit risk to an acceptably low level.

Operationally, planning entails setting a timetable for the audit and defining the nature, timing and extent of the audit procedures. During planning, auditors should assign the members of their team as appropriate and identify other resources that may be required, such as subject experts.
Audit planning should be responsive to significant changes in circumstances and conditions. It is an iterative process that takes place throughout the audit.

**Conducting an audit**

**49. Auditors should perform audit procedures that provide sufficient appropriate audit evidence to support the audit report**

The auditor’s decisions on the nature, timing and extent of audit procedures will impact on the evidence to be obtained. The choice of procedures will depend on the risk assessment or problem analysis.

Audit evidence is any information used by the auditor to determine whether the subject matter complies with the applicable criteria. Evidence may take many forms, such as electronic and paper records of transactions, written and electronic communication with outsiders, observations by the auditor, and oral or written testimony by the audited entity. Methods of obtaining audit evidence can include inspection, observation, inquiry, confirmation, recalculation, reperformance, analytical procedures and/or other research techniques. Evidence should be both sufficient (quantity) to persuade a knowledgeable person that the findings are reasonable, and appropriate (quality) – i.e. relevant, valid and reliable. The auditor’s assessment of the evidence should be objective, fair and balanced. Preliminary findings should be communicated to and discussed with the audited entity to confirm their validity.

The auditor must respect all requirements regarding confidentiality.

**50. Auditors should evaluate the audit evidence and draw conclusions**

After completing the audit procedures, the auditor will review the audit documentation in order to determine whether the subject matter has been sufficiently and appropriately audited. Before drawing conclusions, the auditor reconsiders the initial assessment of risk and materiality in the light of the evidence collected and determines whether additional audit procedures need to be performed.

The auditor should evaluate the audit evidence with a view to obtaining audit findings. When evaluating the audit evidence and assessing materiality of findings the auditor should take both quantitative and qualitative factors into consideration.
Based on the findings, the auditor should exercise professional judgment to reach a conclusion on the subject matter or subject matter information.

**Reporting and follow-up**

**51. Auditors should prepare a report based on the conclusions reached**

The audit process involves preparing a report to communicate the results of the audit to stakeholders, others responsible for governance and the general public. The purpose is also to facilitate follow-up and corrective action. In some SAIs, such as courts of audit with jurisdictional authority, this may include issuing legally binding reports or judicial decisions.

Reports should be easy to understand, free from vagueness or ambiguity and complete. They should be objective and fair, only including information which is supported by sufficient and appropriate audit evidence and ensuring that findings are put into perspective and context.

The form and content of a report will depend on the nature of the audit, the intended users, the applicable standards and legal requirements. The SAI’s mandate and other relevant laws or regulations may specify the layout or wording of reports, which can appear in short form or long form.

Long-form reports generally describe in detail the audit scope, audit findings and conclusions, including potential consequences and constructive recommendations to enable remedial action. Short-form reports are more condensed and generally in a more standardised format.

**Attestation engagements**

In attestation engagements the audit report may express an opinion as to whether the subject matter information is, in all material respects, free from misstatement and/or whether the subject matter complies, in all material respects, with the established criteria. In an attestation engagement the report is generally referred to as the Auditor’s Report.

**Direct engagements**

In direct engagements the audit report needs to state the audit objectives and describe how they were addressed in the audit. It includes findings and
conclusions on the subject matter and may also include recommendations. Additional information about criteria, methodology and sources of data may also be given, and any limitations to the audit scope should be described.

The audit report should explain how the evidence obtained was used and why the resulting conclusions were drawn. This will enable it to provide the intended users with the necessary degree of confidence.

Opinion
When an audit opinion is used to convey the level of assurance, the opinion should be in a standardised format. The opinion may be unmodified or modified. An unmodified opinion is used when either limited or reasonable assurance has been obtained. A modified opinion may be:

- Qualified (except for) – where the auditor disagrees with, or is unable to obtain sufficient and appropriate audit evidence about, certain items in the subject matter which are, or could be, material but not pervasive;
- Adverse – where the auditor, having obtained sufficient and appropriate audit evidence, concludes that deviations or misstatements, whether individually or in the aggregate, are both material and pervasive;
- Disclaimed – where the auditor is unable to obtain sufficient and appropriate audit evidence due to an uncertainty or scope limitation which is both material and pervasive.

Where the opinion is modified the reasons should be put in perspective by clearly explaining, with reference to the applicable criteria, the nature and extent of the modification. Depending on the type of audit, recommendations for corrective action and any contributing internal control deficiencies may also be included in the report.

Follow-up
SAIs have a role in monitoring action taken by the responsible party in response to the matters raised in an audit report. Follow-up focuses on whether the audited entity has adequately addressed the matters raised, including any wider implications. Insufficient or unsatisfactory action by the audited entity may call for a further report by the SAI.
ISSAI 200

Fundamental Principles of Financial Auditing

The International Standards of Supreme Audit Institutions, ISSAI, are issued by the International Organization of Supreme Audit Institutions, INTOSAI. For more information visit www.issai.org.
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INTRODUCTION

1. Professional standards and guidelines are essential for the credibility, quality and professionalism of public sector auditing. The International Standards of Supreme Audit Institutions (ISSAIs) developed by the International Organisation of Supreme Audit Institutions (INTOSAI) aim to promote independent and effective auditing and support the members of INTOSAI in the development of their own professional approach in accordance with their mandates and with national laws and regulations.

2. **ISSAI 100 – Fundamental Principles of Public Sector Auditing** provides the fundamental principles for public sector auditing in general and defines the authority of the ISSAIs. **ISSAI 200 – Fundamental Principles of Financial Auditing** has been developed to address the key principles related to an audit of financial statements in the public sector. It builds on and further develops the fundamental principles of ISSAI 100 to suit the specific context of audits of financial statements, and constitutes the basis for auditing standards related to audits of financial statements. ISSAI 200 should be read and understood in conjunction with ISSAI 100.

3. The main purpose of the ISSAIs on financial audit is to provide INTOSAI members with a comprehensive set of principles, standards and guidelines for the audit of financial statements of public sector entities. In addition to ISSAI 200, the ISSAIs on financial audit comprise the Financial Audit Guidelines (ISSAIs 1000-2999) at level 4 of the ISSAI Framework. A general introduction to these guidelines is given in ISSAI 1000, while ISSAIs 1200 to 1810 each contain Practice Notes issued by INTOSAI to provide guidance on the application of the International Standards on Auditing (ISAs 200 to 810) developed by the International Auditing and Assurance Standards Board (IAASB). Each Practice Note and the corresponding ISA together constitute a guideline in the ISSAI Framework.

4. Financial audit focuses on determining whether an entity’s financial information is presented in accordance with the applicable financial reporting and regulatory framework. The scope of financial audits in the public sector may be defined by
the SAI’s mandate as a range of audit objectives in addition to the objectives of
an audit of financial statements prepared in accordance with a financial reporting
framework. These objectives may include the auditing of:

• states’ or entities’ accounts or other financial reports, not necessarily
  prepared in accordance with a general-purpose financial reporting
  framework;
• budgets, budget sections, appropriations and other decisions on the
  allocation of resources, and the implementation thereof;
• policies, programmes or activities defined by their legal basis or source of
  financing; legally-defined areas of responsibility, such as the responsibilities
  of ministers; and
• categories of income or payments or assets or liabilities

5. When the SAI’s mandate defines such additional audit objectives, the SAI may
also need to consider developing or adopting standards based on the general
fundamental principles of public sector auditing in ISSAI 100 and the
fundamental principles of compliance and performance auditing. The guidance
of the Financial Audit Guidelines on special-purpose frameworks¹, audits of
single financial statements and specific elements, accounts or items of a financial
statement², and reports on summary financial statements³, may also be relevant
for such purposes.

6. This ISSAI provides detailed information on the following:

• The purpose and authority of the Fundamental Principles of Financial
  Auditing
• The framework for auditing financial statements in the public sector
• The elements of an audit of financial statements
• The principles of an audit of financial statements.

¹ISSAI 1800 – Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks.
²ISSAI 1805 – Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement.
PURPOSE AND AUTHORITY OF THE FUNDAMENTAL PRINCIPLES OF FINANCIAL AUDITING

7. ISSAI 200 provides the fundamental principles for an audit of financial statements prepared in accordance with a financial reporting framework. The principles also apply when an SAI is engaged or has responsibility to audit single financial statements and specific elements, accounts or items of a financial statement, or financial statements prepared in accordance with special-purpose financial frameworks, or summary financial statements. Where reference is made in ISSAI 200 to audits of financial statements, this includes responsibilities of this nature.

8. ISSAI 1000 to 1810 on financial audits may be applied as appropriate to these responsibilities. However, auditors are prohibited from making reference to the use of the ISSAI if:
   - the preconditions for an audit in accordance with the ISSAI on financial audit are not in place;
   - the auditor is not able to comply with the authority attached to the ISAs and ISSAI.


10. ISSAI 200 – Fundamental Principles of Financial Auditing represents the core of the detailed auditing standards provided by ISSAI 1000 to 1810 at level 4 of the ISSAI Framework. The principles in ISSAI 200 can be used in three ways:
    - as a basis on which to develop standards,
    - as a basis on which to adopt consistent national standards,
    - as a basis for adoption of the Financial Audit Guidelines as the authoritative standards.

11. Reference to ISSAI 200 in reports should only be made if auditing standards have been developed or adopted that fully comply with all relevant principles of ISSAI.

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4 ISSAI 1210 – Agreeing the Terms of Audit Engagements, paragraphs 6-8
5 ISSAI 1000, paragraphs 37-43.
200. A principle is considered relevant when it deals with the type of audit or combinations of audit types and the circumstances or procedures are applicable. The principles in no way override national laws, regulations or mandates.

12. When adopting or developing audit standards based on the Fundamental Auditing Principles, reference to these in reports may be made by stating:

...We conducted our audit in accordance with [standards], which are based on [or consistent with] the Fundamental Auditing Principles (ISSAIs 100-999) of the International Standards of Supreme Audit Institutions.

13. SAIs adopting the Financial Audit Guidelines on level 4 as their authoritative standards should make reference to these in their reports. Depending on the standards applied and the SAI’s mandate, this can be done in two ways:

   a) In accordance with ISSAIs 1000-1810 – this means full compliance with all relevant ISAs and the additional guidance set out in the INTOSAI Practice Notes;

   b) In accordance with the ISAs – this entails compliance with all relevant ISAs.

ISSAI 100 further explains the authority attached to the ISSAIs.

14. When the level 4 ISSAIs are used as authoritative standards, the public sector auditors should also respect the authority of the ISAs. SAIs are encouraged to strive towards full adoption of the level 4 guidelines as their authoritative standards, as they have been developed to reflect best practice. INTOSAI recognises that in some environments this might not be possible due to the absence of basic administrative structures or because laws or regulations do not establish the same premises for carrying out audits of financial statements in accordance with the Financial Audit Guidelines. Where this is the case, SAIs have the option of developing authoritative standards based on the Fundamental Principles of Financial Auditing.

15. When the level 4 ISSAIs are used as the authoritative standards for an audit of financial statements conducted together with a compliance audit, the public sector auditors should respect the authority of both the Financial Audit Guidelines and the Compliance Audit Guidelines.6
FRAMEWORK FOR FINANCIAL AUDITING

The objective of financial auditing

16. The purpose of an audit of financial statements is to enhance the degree of confidence of intended users in the financial statements. This is achieved through the expression of an opinion by the auditor as to whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework, or — in the case of financial statements prepared in accordance with a fair presentation financial reporting framework — whether the financial statements are presented fairly, in all material respects, or give a true and fair view, in accordance with that framework. Laws or regulations binding public sector audit organisations may prescribe other wordings for this opinion. An audit conducted in accordance with standards based on the INTOSAI Fundamental Principles of Financial Auditing and relevant ethical requirements will enable the auditor to express such an opinion.

17. ISSAI 200 is based on the following objectives, as defined in ISSAI 1200:7
In conducting an audit of financial statements, the overall objectives of the auditor are:

a) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and

b) To report on the financial statements, and communicate the result of the audit, in accordance with the auditor’s findings.

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7 ISSAI 1200, paragraph 11 of ISA 200.
Public sector applications covered by ISSAI 200

Preconditions for an audit of financial statements in accordance with the ISSAIs

18. The auditor should assess whether the preconditions for an audit of financial statements have been met.

19. A financial audit conducted in accordance with the ISSAIs is premised on the following conditions:
   - The financial reporting framework used for preparation of the financial statements is deemed to be acceptable by the auditor.
   - The management of the entity acknowledges and understands its responsibility:
     - For preparation of the financial statements in accordance with the applicable financial reporting framework, including, where relevant, their fair presentation;
     - For such internal control that management deems necessary for the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
     - To provide the auditor with unrestricted access to all information of which it is aware and that is relevant to the preparation of the financial statements.

20. Financial reporting frameworks may be for general use or specific use. A framework designed to meet the information needs of a wide range of users is referred to as a general-purpose framework, while special-purpose frameworks are designed to meet the specific needs of a specific user or group of users. Frameworks may also be referred to as fair presentation frameworks or compliance frameworks. A fair presentation framework requires compliance with the framework but allows, explicitly or implicitly, that it may be necessary to depart from a requirement or to provide additional information in order to achieve fair presentation of the financial statements. The term compliance framework is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and does not acknowledge the possibility of such deviations to achieve a fair presentation.
21. Without an acceptable financial reporting framework, the management will have no appropriate basis for preparing the financial statements and the auditor no suitable criteria for auditing them. Suitable criteria should be formal. For example, in the preparation of financial statements the criteria may be the International Public Sector Accounting Standards (IPSASs), the International Financial Reporting Standards (IFRSs), or other international or national financial reporting frameworks for use in the public sector.

22. A complete set of financial statements for a public sector entity, when prepared in accordance with a financial reporting framework for the public sector, normally consists of:

- a statement of financial position;
- a statement of financial performance;
- a statement of changes in net assets/equity; a cash flow statement;
- a comparison of budget and actual amounts – either as a separate additional financial statement or as a reconciliation;
- notes, comprising a summary of significant accounting policies and other explanatory information;
- in certain environments a complete set of financial statements may also include other reports, such as reports on performance and appropriation reports.

If the financial statements are prepared in accordance with a framework for other accounting bases, such as modified accrual or a cash basis, a complete set of financial statements may not include all of the above.

23. Frameworks prescribed by law or regulation will often be deemed acceptable by the auditor. However, even if deemed unacceptable, such a framework may be allowable if:

- the management agrees to provide the necessary additional disclosures in the financial statements to avoid their being misleading; and
- the auditor’s report on the financial statements includes an Emphasis of matter paragraph drawing users’ attention to such additional disclosures.
If the above conditions are not met, the auditor should evaluate the effect of the misleading nature of the financial statements on the auditor’s report and the opinion, and consider the need to inform the legislature about the matter.

24. Acceptable financial reporting frameworks normally exhibit certain attributes that ensure that the information provided in the financial statements is of value to the intended users:

- **Relevance** – the information provided in the financial statements is relevant to the nature of the audited entity and the purpose of the financial statements;
- **Completeness** – no transactions, events, account balances or disclosures that could affect conclusions based on the financial statements are omitted;
- **Reliability** – the information provided in the financial statements:
  1. where applicable, reflects the economic substance of events and transactions and not merely their legal form; and
  2. results, when used in similar circumstances, in reasonably consistent evaluation, measurement, presentation and disclosure;
- **Neutrality and objectivity** – the information in the financial statements is free from bias;
- **Understandability** – the information in the financial statements is clear and comprehensive and not open to significantly diverse interpretations.

Appendix 2 to ISSAI 1210⁴ may provide further assistance for the auditor in determining whether the financial reporting framework is acceptable.

25. In some public sector audit environments, financial audits are referred to as budget execution audits, which often include the examination of transactions against the budget for compliance and regularity issues. Such audits may be undertaken on a risk basis or with the aim of covering all transactions. In such audit environments there is often no acceptable financial reporting framework. The results of financial transactions may be presented as a comparison between expenditure amounts and budgetary amounts. In environments where such audits are undertaken and there are no financial statements presented in accordance with acceptable financial reporting frameworks.

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⁴ISSAI 1210 – Agreeing the Terms of Audit Engagements.
with an acceptable financial reporting framework, the auditor may conclude that
the preconditions for an audit established by the ISSAIs on financial audit are not
in place. Auditors may thus consider developing standards using the
Fundamental Principles of Financial Auditing as guidance to suit their specific
needs. Where the audit mandate refers to financial audit but does not link this to
financial statements prepared in accordance with a financial reporting
framework, it is proposed that the ISSAIs be considered best available practice
and the spirit of the ISSAIs be implemented through standards devised for the
specific environment. Where the audit mandate refers to audits of single financial
statements and specific elements, accounts or items of a financial statement,
ISSAI 1805\(^9\) may be relevant.

26. The type of audit performed in environments where compliance with authorities
is the main focus of the audit would normally be considered a compliance audit.
*ISSAI 400 – Fundamental Principles of Compliance Auditing* may be a relevant
source of information for the development or adoption of standards for the audit
work. If, on the other hand, the audit mandate allows for a change in audit
procedures and the use of acceptable financial reporting frameworks is
introduced for the preparation of financial statements, the ISSAIs on financial
auditing may be adopted subsequently.

**Audits of financial statements prepared in accordance with special-purpose
frameworks**

27. The principles of ISSAI 200 are applicable to audits of financial statements
prepared in accordance with both general-purpose and special-purpose
frameworks. In addition to preparing general-purpose financial statements, a
public-sector entity may prepare financial statements for other parties (such as
governing bodies, the legislature or other parties with an oversight function),
which may require financial statements tailored to meet their specific
information needs. In some environments financial statements of this kind are the
only financial statements prepared by the public sector entity. Financial
statements prepared for a special purpose are not appropriate for the general
public. Auditors should, therefore, carefully examine whether the financial

\(^9\)ISSAI 1805 – Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts
or Items of a Financial Statement.
reporting framework is designed to meet the financial information needs of a wide range of users (general-purpose framework) or of specific users, or the requirements of a standard-setting body.

28. Special-purpose frameworks relevant to the public sector may include:

- the cash receipts and disbursements basis of accounting for cash flow information that an entity may be required to prepare for a governing body;
- the financial reporting provisions established by an international funding organisation or mechanism;
- the financial reporting provisions established by a governing body, the legislature or other parties that perform an oversight function to meet the requirements of that body; or
- the financial reporting provisions of a contract, such as a project grant.

29. The principles of ISSAI 200 are relevant for audits of financial statements prepared in accordance with such frameworks. In addition to these principles, SAIs may find it useful, when developing or adopting standards based thereon, to consider the requirements and guidance in ISSAI 1800, which deals with special considerations in the application of ISSAIs 1200-1700 to an audit of financial statements prepared in accordance with a special-purpose framework.

Audits of single financial statements and specific elements, accounts or items of a financial statement

30. The principles of ISSAI 200 are also applicable to audits of public-sector entities that prepare financial information, including single financial statements or specific elements, accounts or items of a financial statement, for other parties (such as governing bodies, the legislature or other parties with an oversight function). Such information may come under the audit mandate of the SAI. Auditors may also be engaged to audit single financial statements, or specific elements, accounts or items – such as projects financed by the government – although they are not engaged to audit the complete set of financial statements of the entity concerned.

31. SAIs may also find it useful to consider the requirements and guidance in ISSAI
1805 when developing or adopting standards based on the principles in ISSAI 200. ISSAI 1805 deals with special considerations in the application of the requirements of the ISAs to an audit of a single financial statement or of a specific element, account or item of a financial statement. The single financial statement or the specific element, account or item of a financial statement may be prepared in accordance with a general-purpose or special-purpose framework.

**ELEMENTS OF FINANCIAL AUDITING**

32. Audits of financial statements are defined as assurance engagements, which involve at least three separate parties: an auditor, a responsible party and intended users. The elements of public sector auditing are described in ISSAI 100\(^\text{10}\). ISSAI 200 covers additional aspects of the elements relevant to an audit of financial statements.

*The three parties in financial auditing*

33. In an audit of financial statements, the responsible party is responsible for the subject matter information (normally the financial statements themselves) and may also be responsible for the underlying subject matter (the financial activities reflected in the financial statements). The responsible party is normally the executive branch of government and/or its underlying hierarchy of public-sector entities responsible for the management of public funds, the exercise of authority under the control of the legislature, and the content of the financial statements. These bodies are expected to manage resources and exercise authority in accordance with the decisions and premises of the legislature.

34. Legislators represent the citizens, who are the ultimate users of financial statements in the public sector. The “intended user” is primarily the parliament, which represents the citizens by making decisions and determining the priorities of public finance and the purpose and content of spending and income as part of a public democratic process. The legislature’s decisions and premises may form the basis of the broader perspective of financial audit in the public sector. For public sector entities, legislators and regulators are often the primary users of their financial statements.

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\(^{10}\) ISSAI 100 – Fundamental Principles of Public Sector Auditing.
35. The responsible party and the intended users may be from the same public sector entities or from different bodies. In the first scenario, the supervisory board of a governmental structure may seek assurance about information provided by the management board of the same public sector entity. The relationship between the responsible party and the intended users needs to be viewed within the context of the specific engagement and may differ from more traditionally-defined lines of responsibility.

**Suitable criteria**

36. Criteria are the benchmarks used to evaluate or measure the subject matter, including, where relevant, benchmarks for presentation and disclosure. The criteria used in the preparation of financial statements are normally formal and may be IPSASs, IFRSs or other national financial reporting frameworks for use in the public sector.

**Subject matter information**

37. The financial position, financial performance, cash flows and notes presented in the financial statements (subject matter information) result from applying a financial reporting framework for recognition, measurement, presentation and disclosure (criteria) to a public-sector entity's financial data (subject matter). The term “subject matter information” refers to the outcome of the evaluation or measurement of the subject matter. It is on the subject matter information (e.g. the entity's financial statements) that the auditor gathers sufficient appropriate audit evidence to provide a reasonable basis for expressing an opinion in the auditor’s report.

**Reasonable assurance engagement**

38. Audits of financial statements conducted in accordance with the ISSAIs are reasonable assurance engagements. Reasonable assurance is high, but not absolute, given the inherent limitations of an audit, the result of which is that most of the audit evidence obtained by the auditor will be persuasive rather than conclusive. In general, reasonable assurance audits are designed to result in a conclusion expressed in a positive form, such as “in our opinion the financial
statements present fairly, in all material respects (or give a true and fair view of) the financial position of … and its financial performance and cash flows …” or, in the case of a compliance framework, “in our opinion the financial statements are prepared, in all material respects, in accordance with ...”.

39. Limited assurance engagements, such as review engagements, are not covered at present by the ISSAIs on financial audits. Such engagements provide a lower level of assurance than reasonable assurance engagements, and are designed to result in a conclusion expressed in a negative form, such as “nothing has come to our attention that would cause us to believe that the financial statements were not presented fairly in all material respects”. Auditors performing such engagements may need to apply guidance from outside the financial audit ISSAIs; the fundamental auditing principles in ISSAI 100 may be useful in this regard.

PRINCIPLES OF FINANCIAL AUDITING

General principles

Prerequisites for conducting financial audits

Ethics and independence

40. **The auditor should comply with the relevant ethical requirements, including those pertaining to independence, when carrying out audits of financial statements.**

41. Auditors conducting audits in accordance with the ISSAIs are subject to **ISSAI 30 – Code of Ethics** as applied in the national context. Auditors at SAIs that have adopted the level 4 ISSAIs as their authoritative standards, or that apply the ISAs, are required either to comply with the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA) (the IESBA Code), which establishes fundamental ethical principles for professional accountants, or to adopt national requirements that are at least as demanding; the INTOSAI Code of Ethics applied in the national context may be relevant here. SAIs must therefore adopt the ethical requirements of ISSAI 30 or the IESBA Code in their environment in order to be able to state in their reports that the audit was conducted in accordance with the ISSAIs or the ISAs.
Quality control

42. The auditor should implement quality control procedures at the engagement level that provide reasonable assurance that the audit complies with professional standards and the applicable legal and regulatory requirements, and that the auditor’s report is appropriate in the circumstances.

43. As stated in ISSAI 100, SAIs should adopt quality control procedures in accordance with ISSAI40 – Quality Control for SAIs, which provides the context for the IAASB’s International Standards on Quality Control (ISQC 1) in a public-sector environment. ISQC 1 establishes standards and provides guidance for an organisation’s system of quality control. Although the general purpose and key principles of ISSAI 40 are consistent with ISQC 1, the requirements of ISSAI 40 have been adapted to ensure they are relevant to SAIs.

44. The Head of the SAI or the equivalent collective body has overall responsibility for introducing and maintaining quality control procedures in the SAI, although day-to-day operational responsibility may be delegated to others. For example, any lead auditor with responsibility for an audit engagement would ultimately report to the Head of the SAI.

45. Public sector auditors engaged on audits of financial statements in accordance with standards based on or consistent with the principles of ISSAI 200 are subject to quality control requirements at the engagement level. When developing standards based on ISSAI 200 or adopting standards consistent with ISSAI 200, SAIs should consider formulating requirements related to:

- the need for the lead auditor to take responsibility for overall quality in each audit engagement;
- the need for the lead auditor to ensure that members of the audit team comply with the relevant ethical requirements;
- the need for the lead auditor to form a conclusion regarding compliance with the independence requirements that apply to the audit engagement, and to take appropriate action to eliminate threats to independence;
• the need for the lead auditor to be satisfied that the audit team and any external experts collectively have the appropriate competence and capabilities;
• the need for the lead auditor to take responsibility for the performance of the audit, specifically:
  o leading, supervising and carrying out the audit;
  o ensuring that reviews are conducted in accordance with the SAI’s review policies and procedures.

**Engagement team management and skills**

46. **The auditor should be satisfied that the entire audit team, and any external experts, collectively have the competence and capabilities to:**

   (a) **carry out the audit in accordance with the relevant standards and the applicable legal and regulatory requirements; and**

   (b) **enable the auditor to issue a report that is appropriate in the circumstances.**

47. When addressing the competence and capabilities expected of the team as a whole, the auditor may consider the team’s:

   • Understanding, through appropriate training, and practical experience of audit engagements of a similar nature and complexity;
   • Understanding of professional standards and the applicable legal and regulatory requirements;
   • Technical expertise, including the relevant IT skills and knowledge of specialised areas of accounting or auditing;
   • Knowledge of relevant industries in which the audited organisation operates; Ability to apply professional judgment;
   • Understanding of the SAI’s quality control policies and procedures;
   • Ability to discharge the terms of the audit mandate in the relevant environment, including an understanding of the applicable reporting arrangements, and to report to the legislature or other governing body or in the public interest;
- Skills in the field of performance auditing or compliance auditing, if relevant.

**Principles related to basic audit concepts**

48. ISSAIs 1000-2999 give best practice for the application of the Fundamental Principles of Financial Auditing. However, if an SAI chooses to develop standards based on the fundamental principles, or adopt national standards that are consistent with the principles, the matters covered by this and the following sections should be addressed.

**Audit risk**

49. The auditor should reduce audit risk to an acceptably low level in the circumstances of the audit so as to obtain reasonable assurance as the basis for an opinion expressed in a positive form.

50. The audit risk in an audit of financial statements is the risk that the auditor will express an inappropriate conclusion if the subject matter information is materially misstated. The auditor will reduce the risk to an acceptably low level in the circumstances of the audit to obtain reasonable assurance as the basis for expressing a conclusion in a positive form. To be meaningful, the level of assurance obtained by the auditor must enhance the intended users’ confidence about the subject matter information to a degree that is clearly more than inconsequential.

51. In general, the audit risk depends on the following components:

- The risks of material misstatement consist of inherent risk and control risk:
  
  (a) Inherent risk – the susceptibility of the subject matter information to material misstatement, assuming that there are no related controls;

  (b) Control risk – the risk that a material misstatement could occur and will not be prevented, or detected and corrected, at the appropriate time by related controls. If relevant to the subject matter, some control risk will always exist because of the limitations inherent in the design and operation of internal controls.

- Audit risk is a function of the risks of material misstatement and detection risk:
(c) Detection risk – the risk that the auditor will not detect a material misstatement.

52. The assessment of risks is based on audit procedures to obtain information necessary for that purpose, as well as evidence obtained throughout the audit. The risk assessment is a matter of professional judgment and is not capable of precise measurement. The degree to which the auditor considers each element of risk will depend on the circumstances of the audit.

**Professional judgment and professional skepticism**

53. The auditor should plan and perform the audit with professional skepticism, recognising that circumstances may exist that causes the financial statements to be materially misstated. When planning, performing, concluding and reporting an audit of financial statements, the auditor should exercise professional judgment.

54. The terms “professional skepticism” and “professional judgment” are relevant when formulating requirements regarding the auditor’s decisions about the appropriate response to matters concerning the audit. They express the attitude of the auditor, which includes a questioning mind. These concepts are set out in the ISSAIs on financial audit.

55. The concept of professional judgment is applied by the auditor at all stages of the audit process. It covers the application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, when making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.\(^\text{11}\)

56. Professional judgment is necessary in particular in decisions about:

- materiality and audit risk;
- the nature, timing and extent of the audit procedures used to meet the requirements of the ISSAIs and the ISAs and gather audit evidence;
- evaluating whether sufficient appropriate audit evidence has been

\(^{11}\text{ISSAI 1200, paragraph 13.}\)
obtained, and whether more needs to be done to achieve the auditor’s overall objectives;

- the evaluation of management’s judgment in applying the financial reporting framework applicable to the audited entity;
- the drawing of conclusions from the audit evidence obtained – for example, assessing the reasonableness of the estimates made by management in preparing the financial statements.

57. Professional skepticism is fundamental to all audit engagements. The auditor plans and performs an assurance engagement with an attitude of professional skepticism, recognising that circumstances may exist that cause the subject matter information to be materially misstated. An attitude of professional skepticism means that the auditor makes a critical assessment, with a questioning mind, of the validity of the evidence obtained and is alert to evidence that contradicts or calls into question the reliability of documents or representations by the responsible party. Such an attitude is necessary throughout the audit process so as to reduce the risk of overlooking suspicious circumstances, overgeneralising when drawing conclusions from observations, and using false assumptions to determine the nature, timing and extent of evidence-gathering procedures and evaluate the results thereof.

Materiality

58. **The auditor should apply the concept of materiality in an appropriate manner when planning and performing the audit.**

59. A misstatement is material, individually or when aggregated with other misstatements, if it could reasonably be expected to influence the decisions taken by users on the basis of the financial statements. Materiality has both quantitative and qualitative aspects. In the public sector, it is not limited to economic decisions by users, as decisions as to whether to continue certain government programmes or grant funding may be based on the financial statements. The qualitative aspects of materiality generally play a greater role in the public sector than in other types of entities. The assessment of materiality and the consideration of sensitivity and other qualitative factors in a particular audit are matters for the auditor’s judgment.
60. When determining the audit strategy, the auditor should assess materiality for the financial statements as a whole. If, for one or more classes of transactions, account balances or disclosures, misstatements of amounts less than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users on the basis of the financial statements, the auditor should also determine the materiality level or levels to be applied to the classes of transactions, account balances or disclosures concerned.

61. The auditor should also determine performance materiality for the purposes of assessing the risk of material misstatement and determining the nature, timing and extent of further audit procedures. Planning the audit solely to detect individually material misstatements overlooks the fact that the aggregate of individually immaterial misstatements may cause the financial statements to be materially misstated, and leaves no margin for any undetected misstatements. Performance materiality should be set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements will exceed the materiality threshold for the financial statements as a whole. The determination of performance materiality involves the exercise of professional judgment. It is affected by the auditor’s understanding of the entity, should be updated during the performance of risk assessment procedures, and depends on the nature and extent of misstatements identified in previous audits and thus the auditor’s expectations in terms of misstatements in the current period.

62. The concept of materiality is applied by the auditor in planning and performing the audit, as well as in evaluating the effect of identified misstatements on the audit and of any uncorrected misstatements, including omissions, on the financial statements. The auditor’s opinion deals with the financial statements as a whole, and therefore the auditor is not responsible for detecting misstatements that are not globally material. The auditor should still identify and document quantitative immaterial misstatements, as they may be material due to their nature or when aggregated. Misstatements below the trivial threshold need not be considered.

63. The materiality determined when planning the audit does not necessarily establish an amount below which uncorrected misstatements, individually or in the aggregate, will always be evaluated as immaterial. The circumstances related to some misstatements may cause the auditor to evaluate them as material even if
they are below materiality. Although it is not practicable to design audit procedures to detect misstatements that could be material solely because of their nature, the auditor considers not only the size but also the nature of uncorrected misstatements, and the particular circumstances of their occurrence, when evaluating their effect on the financial statements. The aspects the auditor considers include the sensitive nature of certain transactions or programmes, the public interest, the need for effective legislative oversight and regulation, and the nature of the misstatement or deviation (e.g. if it is a result of fraud or corruption).

Communication

64. The auditor should identify the appropriate contact person(s) within the audited entity’s governance structure and communicate with them regarding the planned scope and timing of the audit and any significant findings.

65. The auditor should communicate with both management and those charged with governance. Communication entails obtaining information relevant to the audit and providing those charged with governance with timely observations that are significant and relevant to their oversight of the financial reporting process. It is important to promote effective two-way communication with those charged with governance.

66. In the public sector, identifying those charged with governance may be a challenge. The audited entity may be part of a larger or broader structure with governance bodies at several organisational levels and across different functions (i.e. vertically and horizontally). As a result, in some cases several distinct groups can be identified as being charged with governance. Furthermore, as an audit in the public sector might involve both financial statement objectives as well as compliance objectives, this too may involve separate governance bodies.

67. Communication should be in writing if the auditor determines that oral communication is not sufficient. The auditor may also be required to communicate with parties other than those within the organisation, such as the legislature, regulators or funding agencies.
68. Written communications need not include all matters arising during the course of the audit. However, written communication is vital for significant audit findings, which auditors are required to communicate to those charged with governance.

69. Auditors in the public sector are often the mandated auditors of the whole or major parts of the government and its administration. In this situation, auditors may have access to information from other audited entities and audits made in their regard, which might be of relevance to those charged with governance. Examples of this might include material errors in transactions with the audited entity that also affect other audited entities, or designs of relevant controls which have provided efficiency gains in other audited entities. Communicating this type of information to those charged with governance may add value to the audit when circumstances permit. However, laws, regulations or ethical requirements may prohibit communication of this type of information.

**Documentation**

70. The auditor should prepare audit documentation that is sufficient to enable an experienced auditor, with no prior knowledge of the audit, to understand the nature, timing and extent of the audit procedures performed to comply with the relevant standards and the applicable legal and regulatory requirements, the results of those procedures and the audit evidence obtained, as well as significant matters arising during the audit, the conclusions reached in their regard, and significant professional judgments made in reaching those conclusions. The documentation should be prepared at the appropriate time.

71. Adequate audit documentation is important for several reasons. It will:

- confirm and support the auditor’s opinions and reports;
- serve as a source of information for preparing reports or answering any enquiries from the audited organization or any other party;
- serve as evidence of the auditor’s compliance with the auditing standards;
- facilitate planning, supervision and review;
- help with the auditor’s professional development;
- help to ensure that delegated work has been satisfactorily executed; and
- provide evidence of work done for future reference.
72. Auditing standards based on the fundamental principles need to include further requirements in relation to documentation in the following areas:

- the timely preparation of documentation;
- the form, content and extent of documentation;
- documentation requirements where the auditor judges it necessary to depart from a relevant requirement in the applied auditing standards;
- documentation requirements where the auditor performs new or additional audit procedures or draws new conclusions after the date of the auditor’s report;
- the assembly of the final audit file.

The level 4 ISSAIs provide additional guidance on adopting requirements and audit documentation.

73. For auditors with a judicial role, such as a court of accounts, documentation forms part of the basis of official rulings. In this environment, due process of law may establish specific and strict requirements to be adhered to regarding confidentiality of documentation in connection with the proceedings of a case. Additionally, as decisions may result in a legally binding public credit, public sector auditors may be subject to supplementary documentation retention requirements.

**Principles related to the audit process**

**Agreeing the terms of the engagement**

74. **The auditor should agree or, if the terms of the engagement are clearly mandated, establish a common understanding of the terms of the audit engagement with management or those charged with governance.**

75. The terms of an audit engagement in the public sector are normally mandated and therefore not subject to requests from, and agreement with, management or those charged with governance. Instead of agreeing the terms formally, public sector auditors may instead choose to establish a common formal understanding of the respective roles and responsibilities of the management and the auditor. Since the public sector auditor is normally engaged by and reports to the legislature, agreements may need to be reached with both the legislature and those charged with governance.
76. The auditor should communicate to the appropriate representatives of those charged with governance the auditor’s responsibilities with regard to the audit of financial statements, including the auditor’s responsibility to form and express an opinion on the financial statements prepared by management under the oversight of those charged with governance.

77. If the terms of the engagement are prescribed in sufficient detail by law or regulation, it may not be necessary to record them in an audit engagement letter or other suitable form of written agreement. One exception may be the statement by management and, where appropriate, those charged with governance, that they acknowledge and understand the responsibilities set out in the specific auditing standards, such as the ISSAIIs and the ISAs. As such engagements are common in the public sector, written agreements on the terms need not be concluded, although they may assist in clarifying the responsibilities of the parties involved.

78. Those charged with governance should also be sent an overview of the planned scope and timing of the audit. The auditor should include views about significant qualitative aspects of the audited entity’s accounting practices, including accounting policies, accounting estimates and financial statement disclosures.

79. SAIs are normally required to carry out audits as mandated. They do not normally have the option of rejecting an assignment, even if the preconditions are not met. Standards developed on the basis of the fundamental principles must provide guidance on suitable action in such circumstances. ISSAI 1210\textsuperscript{12} includes guidance in this regard.

**Planning**

80. **The auditor should develop an overall audit strategy that includes the scope, timing and direction of the audit, as well as an audit plan.**

81. An overall audit strategy will guide the auditor in the development of the audit plan. When developing the audit strategy, the auditor needs to:

   - identify the characteristics of the engagement that define its scope;
   - ascertain the reporting objectives of the engagement so as to plan the timing of the audit and the nature of the communications required;

\textsuperscript{12}ISSAI 1210 – Agreeing the Terms of an Engagement.
consider the factors that, in the auditor’s professional judgment, are significant in directing the engagement team’s efforts;
• consider the results of preliminary activities and, where applicable, whether knowledge gained on other engagements performed by the auditor engaged for the audited entity is relevant;
• ascertain the nature, timing and extent of resources necessary to carry out the engagement; consider the results and knowledge obtained from performance audits and other audit activities relevant to the audited entity, including the implications of previous recommendations;
• consider and assess the expectations of the legislature and other relevant users of the audit report.

82. **The auditor should plan the audit properly to ensure that it is conducted in an effective and efficient manner.**

83. The auditor should prepare an audit plan, which should include a description of:

  • the nature, timing and extent of planned risk assessment procedures;
  • the nature, timing and extent of planned further audit procedures at the assertion level;
  • other planned audit procedures that are necessary so that the engagement complies with the applicable standards. Such procedures may include or describe: a review of the legal framework for the audit; a brief description of the activity, programme or entity to be audited; the reasons for carrying out the audit; the factors affecting the audit, including those determining the materiality of matters to be considered; the audit objectives and scope; the audit approach; the characteristics of the audit evidence to be collected, and the procedures required to collect and analyse evidence; the necessary resources; a timetable for the audit; the form, content and users of the auditor’s report and management letter.

84. Both the overall strategy and the audit plan need to be documented. They must also be updated, as necessary, during the course of the audit.

**Understanding the Audit Entity**

85. **The auditor should have an understanding of the audited entity and its**
environment, including internal control procedures that are relevant to the audit.

86. Understanding the different aspects of the organisation and its environment enables the auditor to effectively plan and perform the audit. The necessary understanding will include:

- the relevant environment, regulations and other external factors, including the applicable financial reporting framework;
- the nature of the audited entity, including its mode of operation, governance structure, funding (to enable the auditor to understand the classes of transactions, account balances and disclosures to be expected in the financial statements), and the selection and application of accounting policies, including the reasons for changes thereto;
- measurement and review of the audited entity’s financial performance;
- decisions initiated outside the audited entity as a result of political processes such as new programmes or budget constraints;
- specific laws and regulations to which the audited entity is subject, and the potential impact of non-compliance with these;
- programme objectives and strategies, which may include public policy elements and therefore have implications for the risk assessment;
- governance structures affected by the legal structure of the audited entity, for example whether the entity is a ministry, department, agency or other type of public sector body.

87. To obtain an understanding of the control environment, it may be relevant to consider the audited entity’s communication and enforcement of integrity and ethical values, its commitment to competence, participation by those charged with governance, the management’s philosophy and operating style, organisational structure, the existence and level of internal audit activity, the assignment of authority and responsibility, and human resource policies and practices.

88. Relevant audit evidence may be obtained through a combination of inquiries and other risk assessment procedures, such as the corroboration of inquiries through observation or inspection of documents. For example, by interviewing
management and employees, the auditor may obtain an understanding of how management shares with staff its views on business practices and ethical behaviour. The auditor may then determine whether relevant controls have been implemented by considering, for example, whether management has a written code of conduct and whether it acts in accordance with the code.

89. As part of the understanding process, the auditor also needs to consider whether the audited entity has a procedure for identifying business risks relevant to financial reporting objectives, and whether it further estimates the significance of those risks by assessing the likelihood of their occurrence. If such a procedure has been established, the auditor needs to obtain an understanding of it, and the results thereof.

90. The auditor’s understanding of internal control relevant to financial reporting may include the following areas:

- the classes of transactions in the audited entity’s operations that are significant to the financial statements;
- the procedures, both manual and using IT, by which those transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial statements;
- the accounting records, supporting information and specific accounts in the financial statements that are used to initiate, record, process and report transactions; this includes procedures for correcting incorrect information and transferring information to the general ledger;
- how the information system captures events and conditions, other than transactions, that are significant to the financial statements;
- the financial reporting process used to prepare the audited entity’s financial statements, including significant accounting estimates and disclosures;
- controls surrounding journal entries, including non-standard journal entries used to record unusual non-recurring transactions or adjustments;
- relevant controls that relate to compliance with authorities;
- controls related to monitoring performance against the budget;
- controls related to transferring budgetary funds to other audited entities;
- controls of classified national security and sensitive personal data, such as tax
and health information; and

- supervision and other controls performed by parties outside the audited entity in areas such as:
  
  - compliance with laws and regulations, such as procurement regulations;
  - execution of the budget;
  - other areas as defined by legislation or audit mandate; and
  - Management accountability.

91. Auditing does not require an understanding of all the controls carried out for each significant class of transactions, account balance and disclosure in the financial statements, or for every assertion relevant to them. However, an understanding of an audited entity’s controls and, if relevant, government-wide controls is not sufficient to test their operating effectiveness unless a degree of automation provides for consistency in the implementation of the controls.

**Risk assessment**

92. The auditor should assess the risks of material misstatement at the financial statement level and the assertion level for classes of transactions, account balances and disclosures so as to provide a basis for further audit procedures.

93. Risk assessment procedures may include:

- inquiries of management and staff within the audited entity who, in the auditor’s judgment, may have information that could assist in identifying risks of material misstatement due to fraud or error;
- analytical procedures;
- observation and inspection.

94. The risks of material misstatement should be identified and assessed at both the financial statement level and the assertion level for classes of transactions, account balances and disclosures so as to provide a basis for designing and performing further audit procedures. For this purpose, the auditor needs to:

- identify risks throughout the process of obtaining an understanding of the
108. Areas in which auditors should be alert to fraud risks leading to material misstatement may include procurement, grants, privatisations, intentional misrepresentation of results or information and misuse of authority or power. When developing standards based on these fundamental principles, the guidance on fraud risk areas in ISSAI 1240 may be of assistance.

109. Requirements for the reporting of fraud in the public sector may be the subject of specific provisions in the audit mandate or related laws or regulations, and the auditor may be required to communicate such issues to parties outside the audited entity, such as regulatory and enforcement authorities. In some environments, there may be a specific obligation to refer indications of fraud to investigative bodies and even to cooperate with such bodies on determining whether fraud or abuse has occurred. In other environments, auditors may be obliged to report circumstances that may indicate the possibility of fraud or abuse to the competent jurisdictional body or to the appropriate part of the government or legislature, such as prosecutors, the police or (if relevant to legislation) affected third parties. Auditors should also consider that the use of public monies tends to raise the profile of fraud. As a result auditors may need to be responsive to public expectations regarding fraud detection.

ISSAI 1240 makes reference to the possibility of extending reporting responsibilities within the public sector so as to address concerns about public accountability.

**Going-concern considerations**

110. The auditor should consider whether there are events or conditions that may cast significant doubt on the audited entity’s ability to continue as a going concern.

111. Financial statements are normally prepared on the assumption that the audited entity is a going concern and will continue to meet its statutory obligations for the foreseeable future. In assessing whether the going-concern assumption is appropriate, those responsible for preparation of the financial statements take into account all available information for the foreseeable future. General-purpose financial statements are prepared on a going-concern basis unless the legislature has decided to liquidate the audited entity or that it should cease operation.
112. The going-concern concept may have little or no relevance for “ordinary” public sector entities such as those funded through appropriations on the government budget. When such organisations are abolished or merged with others, their liabilities and assets are usually taken over by other public sector entities. For some types of entities, such as government business enterprises and joint ventures with other principals (including private sector entities operating in legal forms that provide for limited owner liability), this may not be the case. The responsibility for implementing government programmes may also be contracted out to private sector organisations, such as NGOs and private companies, but the programmes may still be audited by the SAI. There is a general trend towards outsourcing, making the going-concern concept and the auditor’s judgment in this regard increasingly relevant to public sector audit.

113. Some financial reporting frameworks contain an explicit requirement for management to make a specific assessment of the audited entity’s ability to continue as a going concern, as well as standards relating to the matters to be considered and disclosures to be made in this regard.

Since the going-concern assumption is a fundamental principle in the preparation of financial statements, management must assess the audited entity’s ability to continue as a going concern even if the financial reporting framework does not explicitly require them to do so.

114. The auditor should obtain sufficient appropriate audit evidence about the suitability of management’s use of the going-concern assumption in the preparation and presentation of financial statements, and should conclude as to whether there is any material uncertainty about the audited entity’s ability to continue as a going concern. If the financial statements were prepared on a going-concern basis but, in the auditor’s judgment, the use of the going-concern assumption is inappropriate, the auditor should express an adverse opinion. If the auditor concludes that use of the going-concern assumption is appropriate in the circumstances and adequate disclosure is made in the financial statements, but that a material uncertainty exists, the auditor should express an unmodified opinion and include an Emphasis of Matter paragraph. If such disclosure is not
made in the financial statements, the auditor should express a qualified or adverse opinion, as appropriate, in accordance with ISSAI 1705\textsuperscript{13}.

115. The degree of consideration will depend on the facts in each case, and assessments of the going-concern assumption are not predicated on the solvency test usually applied to business enterprises. In certain circumstances, while the usual going-concern tests of liquidity and solvency may appear unfavourable, other factors may suggest that the audited entity is nonetheless a going concern. For example:

- In assessing whether a government is a going concern, the power to levy rates or taxes may enable some audited entities to be considered as going concerns even though they may operate for extended periods with negative net assets/equity; and

- Assessment of an individual audited entity’s statement of financial position at the reporting date may suggest that use of the going-concern assumption in the preparation of its financial statements is not appropriate. However, there may be multi-year funding agreements or other arrangements in place that will ensure the continued operation of the audited entity.

116. Generally speaking, determining whether the going-concern assumption is appropriate is relevant to individual audited entities rather than to government as a whole. In the case of individual audited entities, before concluding that use of the going-concern assumption is appropriate, those responsible for the preparation of financial statements may need to consider a wide range of factors surrounding current and expected performance, the potential or announced restructuring of organisational units, revenue estimates or the likelihood of continued government funding, and potential sources of replacement financing.

117. When performing risk assessment procedures the auditor should consider whether there are any events or conditions that may cast significant doubt on the audited entity’s ability to continue as a going concern. In forming a view of the audited entity’s ability to continue its operations, the auditor should examine two separate but sometimes overlapping factors:

- the greater risk associated with changes in policy direction (for example, where there is a change in government); and

\textsuperscript{13}ISSAI 1705 – Modifications to the Opinion in the Independent Auditor’s Report.
the less common operational, or business, risk (for example, where an audited entity has insufficient working capital to continue its operations at the existing level).

Considerations relating to laws and regulations in an audit of financial statements

118. **The auditor should identify the risks of material misstatement due to direct and material non-compliance with laws and regulations.** Identification of such risks should be based on a general understanding of the legal and regulatory framework applicable to the specific environment in which the audited entity operates, including how the audited entity complies with that framework.

The auditor should obtain sufficient appropriate audit evidence regarding compliance with the laws and regulations that are generally recognised to have a direct and material effect on the determination of material amounts and disclosures in financial statements.

119. The auditor is expected to obtain reasonable assurance as to whether the financial statements, taken as a whole, are free from material misstatement, whether due to fraud or error. However, the auditor is not responsible for preventing non-compliance and cannot be expected to detect all breaches of laws and regulations.

120. When conducting an audit of financial statements in accordance with standards based on or consistent with ISSAI 200, the auditor needs to have an understanding of the legal and regulatory framework applicable to the entity.

121. The effect of laws and regulations on the financial statements varies considerably. The laws and regulations to which an audited entity is subject constitute the applicable legal and regulatory framework. The provisions of some laws or regulations have a direct effect on the financial statements in that they determine the nature of reported amounts and disclosures. While other laws or regulations are to be complied with by management or set the terms under which the audited entity is allowed to conduct its operations, they do not have a direct effect on the entity’s financial statements.
122. Non-compliance with laws and regulations may result in fines, litigation or other consequences for the audited entity that may have a material effect on the financial statements.

123. In the public sector, the distribution by an agency of grants and subsidies may be subject to specific laws and regulations that will have a direct impact on the financial statements. Often the financial reporting framework may also include information such as a budget report, appropriation report or performance report. Where the financial reporting framework includes such information, the auditor may need to consider specific laws and regulations that could affect it directly or indirectly.

124. Matters involving non-compliance with laws and regulations that come to the auditor's attention during the course of the audit should be communicated to those charged with governance, save where the matters are clearly inconsequential. However, the audit mandate, or obligations for public-sector entities arising from legislation, regulation, ministerial directives, government policy requirements or resolutions by the legislature, may result in additional objectives, such as the responsibility to report all instances of non-compliance with authorities, even where clearly inconsequential.

125. This broader scope of reporting may, for example, include the obligation to express a separate opinion as to the audited entity’s compliance with laws and regulations, or to report cases of non-compliance. These additional objectives are dealt with in ISSAI 400 – Fundamental Principles of Compliance Auditing and the related guidelines.14 However, even where there are no such additional objectives, there may be general public expectations in regard to the auditors’ reporting of non-compliance with authorities. The auditors should therefore bear such expectations in mind and be alert to instances of non-compliance.

Audit evidence

126. The auditor should perform audit procedures in such a way as to obtain sufficient appropriate audit evidence and thus draw conclusions on which to base the auditor’s opinion.

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14ISSAI 4000 – Compliance Audit Guidelines – General Introduction and ISSAI 4200 – Compliance Audit Guidelines Related to the Audit of Financial Statements
127. Audit procedures should be appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence. Audit evidence comprises information contained in the accounting records underlying the financial statements and from other sources. The auditor should consider both the relevance and the reliability of the information to be used as audit evidence. An audit of financial statements does not involve the authentication of documentation, nor is the auditor trained as or expected to be an expert in such authentication. However, the auditor should consider the reliability of the information to be used as evidence, including photocopies, facsimiles, filmed, digitised or other electronic documents, and take account, where relevant, of controls over their preparation and maintenance.

128. Audit evidence should be sufficient and appropriate. Sufficiency is a measure of the quantity of evidence, while appropriateness relates to the quality of evidence – its relevance and reliability. The quantity of evidence required depends on the risk of material misstatement of the subject matter information (the greater the risk, the more evidence is likely to be required) and on the quality of such evidence (the higher the quality, the less may be required). Accordingly, the sufficiency and appropriateness of evidence are interrelated. However, merely obtaining more evidence does not compensate for its poor quality.

129. The reliability of evidence is influenced by its source and nature, and is dependent on the specific circumstances in which the evidence was obtained. Generalisations about the reliability of various kinds of evidence can be made – but with important exceptions. Even when evidence was obtained from sources external to the audited entity, such as external confirmations, circumstances may exist that could affect the reliability of the information. While recognising that exceptions may exist, the following generalisations about the reliability of evidence may be useful:

- Evidence is more reliable when it is obtained from independent sources outside the audited entity.

- Evidence that is generated internally is more reliable when the related controls are effective.

- Evidence obtained directly by the auditor (for example, through
observation of the application of a control) is more reliable than evidence obtained indirectly or by inference (for example, through inquiry into the application of a control).

- Evidence is more reliable when it exists in documentary form, whether paper, electronic, or other media (for example, a simultaneous written record of a meeting is more reliable than a subsequent oral report of what was discussed).

- Evidence provided by original documents is more reliable than evidence provided by photocopies or facsimiles.

130. Greater assurance is ordinarily provided by consistent evidence obtained from different sources, or of a different nature, than by items of evidence considered individually. In addition, by obtaining evidence from different sources or of a different nature, it may be possible to identify individual items of evidence that are unreliable.

131. Audit evidence may be obtained by testing accounting records. As well as information that supports and corroborates management assertions, account should be taken of any information that contradicts those assertions. In the case of financial statements in the public sector, management may often assert that transactions and events were carried out in accordance with the legislation or due authority, and such assertions may well lie within the scope of a financial audit. It may also be necessary for auditors in the public sector to consider the requirements and guidance in the Fundamental Principles of Compliance Auditing and the related guidelines\(^\text{15}\)when developing or adopting standards in such cases.

132. When adopting or developing auditing standards, SAIs should also consider the need for requirements to obtain sufficient and appropriate audit evidence in relation to:

- the use of external confirmations as audit evidence;
- audit evidence from analytical procedures and different audit sampling techniques; audit evidence from the use of fair value measurement, if relevant;

\(^\text{15}\)ISSAIs 400, 4000 and 4200
• audit evidence when the audited entity has related parties;
• audit evidence from the audited entity’s use of service organisations;
• audit evidence from using the work of internal audit functions or, when allowed by law or regulation and considered relevant, the direct assistance of internal auditors;
• audit evidence from external experts;
• the use of written representations to support audit evidence.

Further guidance on such procedures and requirements are included in the level 4 ISSAIs, which may be of assistance for SAIs when developing further requirements in these areas.

133. Auditors in certain environments, such as a court of accounts, may be subject to laws and regulations requiring them to understand and follow precise procedures related to rules of evidence. Public sector auditors should familiarise themselves with any such policies and procedures that describe additional requirements relating to audit evidence and are designed to ensure compliance with the applicable rules.

**Consideration of subsequent events**

134. The auditor should obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor’s report that require an adjustment to, or disclosure in, the financial statements have been identified. The auditor should also respond appropriately to facts that became known after the date of the auditor’s report and which, had they been known at that date, might have caused the auditor to amend the auditor’s report.

135. Procedures should be designed, as nearly as possible, to cover the period from the date of the financial statements to the date of the auditor’s report. The auditor is not, however, expected to perform additional audit procedures on matters to which previous audit procedures have provided satisfactory conclusions. Financial statements may be affected by certain types of subsequent events (those occurring after the date of the financial statements). Many financial
reporting frameworks specifically refer to such events. Ordinarily, two types of event are identified:

a) Events that provide evidence of conditions that existed at the date of the financial statements; and

b) Events that provide evidence of conditions that arose after the date of the financial statements.

136. Procedures for obtaining sufficient appropriate audit evidence may include:

- steps to obtain an understanding of any procedures established by management to ensure that subsequent events are identified;
- inquiries of management;
- scrutiny of minutes;
- scrutiny of the entity’s most recent interim financial statements, if any.

When making inquiries of management, auditors may need to consider subsequent events that are relevant to the government entity’s ability to fulfill its programme objectives and may therefore affect the presentation of performance information in the financial statements.

137. The auditor is under no obligation to perform any audit procedures on the financial statements after the date of the auditor’s report. However, if, after the date of the auditor’s report but before the financial statements have been issued, a fact becomes known to the auditor that, had it been known at the date of the auditor’s report, might have caused an amendment to the report, appropriate action should be taken. Such action may include:

- discussing the matter with the management and, where appropriate, those charged with governance,
- determining whether the financial statements need amendment and, if so,
- inquiring how the management intends to address the matter in the financial statements.

138. If the management does not take the necessary steps to ensure that anyone in receipt of the financial statements, where already issued, is informed of the situation, and does not amend the financial statements in circumstances where the auditor believes they need to be amended, the auditor should notify the management and those charged with governance that the auditor will seek to
prevent future reliance on the auditor’s report. This may entail seeking legal advice and reporting to the appropriate statutory body. Further guidance is included in ISSAI 1560\textsuperscript{16}.

\textit{Evaluating misstatements}

139. \textbf{The auditor should keep a full record of misstatements identified during the audit, and communicate to management and those charged with governance, as appropriate and on a timely basis, all misstatements recorded during the course of the audit.}

140. Uncorrected misstatements should be evaluated for materiality, individually or in aggregate, to determine what effect they may have on the opinion to be given in the auditor’s report.

141. The auditor should invite the management to correct misstatements, and if the management refuses to correct some or all communicated misstatements the auditor should find out why. When evaluating whether the financial statements as a whole are misstated, the auditor should consider the reasons given for not making corrections. Those charged with governance should be notified of uncorrected misstatements and the effect that they may have, individually or in aggregate, on the opinion in the auditor’s report. The auditor’s notification should individually identify uncorrected material misstatements in classes of transactions, account balances or disclosures.

142. Misstatements that are clearly trivial need not normally be communicated, save where the auditor is required by mandate to report all misstatements. The auditor needs to determine whether uncorrected misstatements are material, individually or in the aggregate. To this end, the auditor should consider;

- the size and nature of the misstatements, in relation both to particular classes of transactions, account balances or disclosures and to the financial statements as a whole, and the particular circumstances of their occurrence; and
- the effect of uncorrected misstatements from prior periods on the relevant classes of transactions, account balances or disclosures, and on the financial statements as a whole.

\textsuperscript{16}ISSAI 1560 – Subsequent Events.
Further guidance on evaluating misstatements is included in ISSAI 1450\(^\text{17}\).

**Forming an opinion and reporting on the financial statements**

143. The auditor should form an opinion based on an evaluation of the conclusions drawn from the audit evidence obtained, as to whether the financial statements as a whole are prepared in accordance with the applicable financial reporting framework. The opinion should be expressed clearly in a written report that also describes the basis for the opinion.

144. The objectives of a financial audit in the public sector are often broader than expressing an opinion as to whether the financial statements have been prepared, in all material respects, in accordance with the applicable financial reporting framework. The audit mandate, or legislation, regulation, ministerial directive, government policy requirements or resolutions by the legislature, may include additional objectives of equal importance to the opinion on the financial statements. These additional objectives may include audit and reporting responsibilities relating, for example, to any findings of non-compliance with authorities. However, even where no additional objectives are set, there may be general public expectations in regard to the reporting of non-compliance with authorities or the effectiveness of internal controls.

145. Auditors with responsibilities relating to reporting on compliance or non-compliance with authorities may consider the Fundamental Principles of Compliance Auditing and related guidelines\(^\text{18}\).

146. In order to form an opinion, the auditor must first conclude whether reasonable assurance has been obtained as to whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. The conclusion should take into account:

a) Whether sufficient appropriate evidence has been obtained;

b) Whether uncorrected misstatements are material, individually or in aggregate; and

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\(^{17}\)ISSAI 1450 – Evaluation of Misstatements Identified during the Audit.
c) The auditor’s evaluations of the following points, which are taken into consideration when determining the form of the opinion:

- Whether the financial statements are prepared in all material respects, in accordance with requirements of the applicable financial reporting framework, including consideration of the qualitative aspects of the entity’s accounting practices, such as possible bias in management’s judgments;
- Whether the financial statements adequately disclose the significant accounting policies selected and applied;
- Whether the accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;
- Whether the accounting estimates made by management are reasonable;
- Whether the information presented in the financial statements is relevant, reliable, comparable, and understandable;
- Whether the financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements;
- Whether the terminology used in the financial statements, including the title of each financial statement, is appropriate;
- Whether the financial statements adequately refer to or describe the applicable financial reporting framework.

d) Where the financial statements have been prepared in accordance with a fair presentation framework, the conclusion should also consider whether the financial statements achieve fair presentation:

- in terms of overall presentation, structure and content;
- whether the financial statements, including the related notes, fairly present the underlying transactions and events.

**Form of opinion**

147. The auditor should express an unmodified opinion if it is concluded that the financial statements are prepared, in all material respects, in accordance with the applicable financial framework.
If the auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, or is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement, the auditor should modify the opinion in the auditor’s report in accordance with the section on “Determining the type of modification to the auditor’s opinion”.

148. If financial statements prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation, the auditor should discuss the matter with the management and, depending on the requirements of the applicable financial reporting framework and how the matter is resolved, determine whether it is necessary to modify the audit opinion.

Elements required in the auditor’s report

149. The auditor’s report should be in written form and contain the following elements:

- A title that clearly indicates that it is the report of an independent auditor;
- An addressee as required by the circumstances of the engagement;
- An introductory paragraph that (1) identifies whose financial statements have been audited, (2) states that the financial statements have been audited, (3) identifies the title of each statement comprising the financial statements, (4) refers to the summary of significant accounting policies and other explanatory information, and (5) specifies the date or period covered by each financial statement comprising the financial statements;
- A section with the heading “Management’s responsibility for the financial statements”, stating that the management is responsible for the financial statements in accordance with the applicable financial reporting framework and for internal controls to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error;
- A section with the heading “Auditor’s responsibility”, stating that the responsibility of the auditor is to express an opinion based on the audit of the financial statements, and describing an audit as involving procedures to obtain audit evidence about the amounts and disclosures in the financial statements, the procedures selected being dependent on the auditor’s
judgment as to, *inter alia*, the risks of material misstatement of the financial statements, whether due to fraud or error. In making the risk assessment, the auditor should consider internal controls relevant to the entity’s preparation of the financial statements and design audit procedures that are appropriate in the circumstances. This section should also refer to the evaluation of the appropriateness of the accounting policies used and the reasonableness of the accounting estimates made by the management, as well as the overall presentation of the financial statements. It should be stated whether the auditor believes that the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor’s opinion;

- A section with the heading “Opinion” which should use one of the following equivalent phrases when expressing an unmodified opinion on the financial statements prepared in accordance with a fair presentation framework:
  
  - *The financial statements present fairly, in all material respects,... in accordance with [the applicable reporting framework];* or
  
  - *The financial statements give a true and fair view of ... in accordance with [the applicable financial reporting framework].*

When expressing an unmodified opinion on financial statements prepared in accordance with a compliance framework, the auditor’s opinion should be that the financial statements are prepared, in all material respects, in accordance with [the applicable financial reporting framework].

If the reference to the applicable financial reporting framework is not to the IPSASs or the IFRSs, the auditor’s opinion should identify the jurisdiction of origin of the framework.

- If required, or as determined by the auditor, a section with the heading “Report on other legal and regulatory requirements” or otherwise as appropriate to the content of the section, addressing other reporting responsibilities in the auditor’s report on the financial statements that are in addition to the requirement to report on the financial statements.

- The auditor’s signature.

- The date on which the auditor obtained sufficient appropriate evidence on which
to base the auditor’s opinion on the financial statements, including evidence that:
   o all the statements comprising the financial statements, including the related notes, have been prepared; and
   o those with the recognised authority have asserted that they take responsibility for the financial statements.

• The location in the jurisdiction where the auditor practises.

150. In addition to the opinion, the auditor may be required by law or regulation to report observations and findings which have not affected the opinion and any recommendations made as a result thereof. These elements should be clearly separate from the opinion.

**Modifications to the opinion in the auditor’s report**

151. The auditor should modify the opinion in the auditor’s report if it is concluded that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, or if the auditor was unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement. Auditors may issue three types of modified opinions: a qualified opinion, an adverse opinion and a disclaimer of opinion.

**Determining the type of modification to the auditor’s opinion**

152. The decision regarding which type of modified opinion is appropriate depends upon:
   • The nature of the matter giving rise to the modification – that is, whether the financial statements are materially misstated or, in the event that it was impossible to obtain sufficient appropriate audit evidence, may be materially misstated; and
   • The auditor’s judgment about the pervasiveness of the effects or possible effects of the matter on the financial statements.

153. The auditor should express a qualified opinion if: (1) having obtained sufficient appropriate audit evidence, the auditor concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or (2) the auditor was unable to obtain sufficient appropriate audit evidence on which to base an opinion, but concludes that the effects on the financial statements of any undetected misstatements could be material but not pervasive.
154. The auditor should express an adverse opinion if, having obtained sufficient appropriate audit evidence, the auditor concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

155. The auditor should disclaim an opinion if, having been unable to obtain sufficient appropriate audit evidence on which to base the opinion, the auditor concludes that the effects on the financial statements of any undetected misstatements could be both material and pervasive. If, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the audit scope that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor should request that management remove the limitation.

156. If expressing a modified audit opinion, the auditor should also modify the heading to correspond with the type of opinion expressed. ISSAI 1705 provides additional guidance on the specific language to use when expressing a modified opinion and describing the auditor’s responsibility. It also includes illustrative examples of reports.

Emphasis of Matter paragraphs and Other Matters paragraphs in the auditor’s report

157. If the auditor considers it necessary to draw users’ attention to a matter presented or disclosed in the financial statements that is of such importance that it is fundamental to their understanding of the financial statements, but there is sufficient appropriate evidence that the matter is not materially misstated in the financial statements, the auditor should include an Emphasis of Matter paragraphs in the auditor’s report. Emphasis of Matter paragraphs should only refer to information presented or disclosed in the financial statements.

158. An Emphasis of Matter paragraphs should:

- be included immediately after the opinion;
- use the Heading “Emphasis of Matter” or another appropriate heading;

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include a clear reference to the matter being emphasised and indicate where the relevant disclosures that fully describe the matter can be found in the financial statements; and

indicate that the auditor’s opinion is not modified in respect of the matter emphasised.

159. If the auditor considers it necessary to communicate a matter, other than those that are presented or disclosed in the financial statements, which, in the auditor’s judgment, is relevant to users’ understanding of the audit, the auditor’s responsibilities or the auditor’s report, and provided this is not prohibited by law or regulation, this should be done in a paragraph with the heading “Other Matter,” or another appropriate heading. This paragraph should appear immediately after the opinion and any Emphasis of Matter paragraph.

160. If the auditor expects to include either or both of these paragraphs in the auditor’s report, the auditor should communicate that expectation and the wording of such paragraphs to those charged with governance. The auditor may also be required or decide to notify other parties, such as the legislature, in addition to those charged with governance.

161. Public sector audit mandates or expectations may expand the circumstances in which it would be relevant to include an Emphasis of Matter paragraph (concerning a matter properly disclosed in the financial statements) or an Other Matters paragraph (concerning information not disclosed in the financial statements).

*Comparative information – corresponding figures and comparative financial statements*

162. Comparative information’ refers to amounts and disclosures included in the financial statements in respect of one or more prior periods. The auditor should determine whether the financial statements include the comparative information required by the applicable financial reporting framework, and whether such information is correctly classified. To accomplish this, the auditor should evaluate whether:

- the comparative information agrees with the amounts and other disclosures that were presented in the prior period or, where appropriate, have been restated; and
• the accounting policies reflected in the comparative information are consistent with those applied in the current period or, if there have been changes in accounting policies, whether those changes have been properly accounted for and adequately presented and disclosed.

163. If the auditor becomes aware, during the current period, of a possible material misstatement in the comparative information, the auditor should perform such additional audit procedures as are necessary in the circumstances to obtain sufficient appropriate audit evidence as to whether a material misstatement exists.

164. Comparative information may take the form of corresponding figures which are included as an integral part of the current period financial statements and are intended to be read only in relation to the amounts and other disclosures relating to the current period. When corresponding figures are presented, the auditor’s opinion should not refer to them save in the following circumstances:

• If the auditor’s report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion or an adverse opinion, and if the matter which gave rise to the modification is unresolved, the auditor should express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements, modified with respect to the corresponding figures included therein.

• If the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements on which an unmodified opinion was issued, and if the corresponding figures have not been properly restated or appropriate disclosures have not been made, the auditor should express a qualified opinion or an adverse opinion in the auditor’s report on the current period financial statements.

• If the prior period financial statements were not audited, the auditor should state in an Other Matter paragraph that the corresponding figures are unaudited.

The auditor should consider these circumstances using the current year for purposes of comparison and the materiality considerations for the current year. If
comparative financial statements are presented, the auditor’s opinion should refer to each period for which they are presented and on which an audit opinion is expressed.

165. When reporting on prior period financial statements in connection with the current period audit, if the auditor’s current opinion on the prior period financial statements differs from the opinion previously expressed, the auditor should disclose the substantive reasons for the difference in an Other Matters paragraph.

166. If the financial statements of the prior period were audited by a predecessor auditor, in addition to expressing an opinion on the current period financial statements the auditor should state in an Other Matter paragraph:

- that the financial statements of the prior period were audited by the predecessor auditor;
- the type of opinion expressed by the predecessor auditor and, if the opinion has been modified, the reasons for doing so; and
- the date of the previous report (unless the predecessor auditor’s report on the prior period financial statements is reissued with the present financial statements).

167. If the auditor concludes that the prior period financial statements on which the predecessor auditor reported without modification are affected by a material misstatement, the auditor should communicate the misstatement to the appropriate level of management and those charged with governance and request that the predecessor auditor be informed. If the prior period financial statements are amended and the predecessor auditor agrees to issue a new auditor's report on the amended financial statements, the auditor should report only on the current period.

168. If the prior period financial statements were not audited, the auditor should state in an Other Matter paragraph that the comparative financial statements are unaudited. Doing this does not exempt the auditor from the need to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period financial statements.
Further guidance on comparative information is included in ISSAI 1710.\textsuperscript{20}

*The auditor’s responsibilities in relation to other information in documents containing audited financial statements*

169. The auditor should read the other information in order to identify any material inconsistencies or material misstatement of fact with the audited financial statements. If, on reading the other information, the auditor identifies a material inconsistency or material misstatement of fact, the auditor should determine whether the audited financial statements or the other information needs to be revised. The action the auditor should take may include modifying of the auditor’s opinion, withholding the auditor’s report, withdrawing from the engagement (in the rare cases where this is possible in the public sector), notifying those charged with governance, or including an Other Matter paragraph in the auditor’s report.

170. If the auditor identifies a material inconsistency or material misstatement of fact that the management refuses to correct, the auditor is required to notify those charged with governance. Auditors may also be required or decide to notify other parties, such as the legislature, in addition to those charged with governance. Further guidance on the auditor’s responsibilities in relation to other documents is included in ISSAI 1720.\textsuperscript{21}

*Special considerations – audits of financial statements prepared in accordance with special-purpose frameworks*

171. The auditor is required to determine the acceptability of the financial reporting framework that was applied when preparing the financial statements. In an audit of special-purpose financial statements, the auditor should obtain an understanding of:

- the purpose for which the financial statements are prepared;
- the intended users; and
- the steps taken by management to determine that the applicable financial reporting framework is acceptable in the circumstances.

\textsuperscript{20}ISSAI 1710 – Comparative Information – Corresponding Figures and Comparative Financial Statements.

\textsuperscript{21}ISSAI 1720 – The Auditor’s Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements.
172. In planning and performing an audit of special-purpose financial statements, the auditor should determine whether the circumstances of the engagement require special consideration to be given to application of the ISSAIs.

173. When forming an opinion and reporting on special-purpose financial statements, the auditor should comply with the same requirements as for general-purpose financial statements. The auditor’s report on special-purpose financial statements should:

- describe the purpose for which the financial statements have been prepared; and
- make reference to the management’s responsibility for determining that the applicable financial reporting framework is acceptable in the circumstances where the management has a choice of frameworks to use in preparing the financial statements.

174. The auditor should include an Emphasis of Matter paragraph alerting users to the fact that the financial statements have been prepared in accordance with a special-purpose framework and that, as a result, they may not be suitable for another purpose.

175. Further guidance on the special considerations in relation to audits of financial statements prepared in accordance with special-purpose frameworks is included in ISSAI 1800.

**Special considerations – audits of single financial statements and specific elements, accounts or items of a financial statement**

176. In the case of an audit of a single financial statement, or of a specific element of a financial statement, the auditor should first determine whether the audit is practicable. The fundamental principles apply to audits of a single financial statement, or of a specific element of a financial statement, irrespective of whether the auditor is also engaged to audit the entity’s complete set of financial statements. If the auditor is not also engaged to audit the complete financial statements, the auditor should determine whether the audit of a single financial

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22 ISSAI 1800 – Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks.
statement, or of a specific element of those financial statements, is in accordance with the fundamental principles set out in the relevant auditing standards.

177. The auditor should also determine whether application of the financial reporting framework will result in a presentation that provides adequate disclosure to enable the intended users to understand the information in the financial statement or the element thereof, as well as the effect of material transactions and events on that information.

178. The auditor should consider whether the expected form of opinion is appropriate in the circumstances of the engagement, and should adapt the reporting requirements as necessary.

179. If the auditor is engaged to report on a single financial statement, or on a specific element of a financial statement, in conjunction with an engagement to audit the entity’s complete set of financial statements, the auditor should express a separate opinion for each engagement.

180. If the opinion in the auditor’s report on an entity’s complete financial statements is modified, or the report includes an Emphasis of Matter paragraph or Other Matter paragraph, the auditor should determine the effect this may have on the auditor’s report on a single financial statement or a specific element of a financial statement. Where appropriate, the auditor should modify the opinion or include an Emphasis of Matter paragraph or Other Matter paragraph in the auditor’s report on the single financial statement or specific element of a financial statement.

181. If the auditor concludes that it is necessary to express an adverse opinion or disclaim an opinion on the entity’s complete financial statements, the auditor may not issue an unmodified auditor’s opinion on a single financial statement or a specific element thereof. This is because an unmodified opinion would contradict the adverse opinion or disclaimer of opinion on the financial statements as a whole. Additional requirements and guidance on issuing these reports in conjunction with the opinion on the complete set of financial statements are provided in ISSAI 1805.

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23ISSAI 1805 – Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement.
Considerations relevant to audits of group financial statements (including whole-of-government financial statements)

182. Auditors engaged to audit group financial statements should obtain sufficient appropriate audit evidence regarding the financial information of all components and the consolidation process to express an opinion as to whether the whole-of-government financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

183. The principles of ISSAI 200 apply to all public sector audits of financial statements, whether for components of government or the whole of government. In situations where the auditor is engaged to audit group financial statements, such as whole-of-government accounts, specific requirements and considerations may apply. The auditor carrying out an audit of group financial statements is referred to as the group auditor. The group auditor should establish a group audit strategy and develop a group audit plan. The principles for understanding the entity should include an understanding of the group, its components and their environments, including group-wide controls, as well as the consolidation process. The understanding thus obtained should be sufficient to confirm or revise the initial identification of components that are likely to be significant for the group financial statements, and to assess the risks of material misstatement, whether due to fraud or error, of the group financial statements.

184. Components of group financial statements may include agencies, departments, bureaus, corporations, funds, component units, districts, joint ventures and non-governmental organisations. Components may be considered to be significant:

- due to their individual financial significance;
- if, due to their specific nature or circumstances, they are likely to include significant risks of material misstatement of the group financial statements;
- if they involve matters that have heightened public sensitivity, such as national security issues, donor-funded projects or reporting on tax revenue.

185. In the public sector, it can be difficult to decide which components to include in
the group financial statements. Application of the financial reporting framework may result in the exclusion of a specific type of agency, department, bureau, corporation, fund, district, joint venture or non-governmental organisation. In such cases, if the group auditor believes that this outcome would result in a misleading presentation of the group financial statements, the group auditor may consider, in addition to the impact on the auditor’s report, the need to communicate the matter to the legislature or other appropriate regulatory bodies.

186. In certain situations the financial reporting framework may not provide specific guidance for the inclusion, or exclusion, of a specific type of agency, department, bureau, corporation, fund, district, joint venture or non-governmental organisation in the group financial statements. In such cases, the group auditor may participate in discussions between group management and component management to determine whether the treatment of the component in the group financial statements will result in a fair presentation. This difficulty may have implications for using the work of component auditors. It is also possible that the group management will not agree to include the component in the group financial statements, which may in turn limit the ability of the group auditor to communicate with and use the work of the component auditor.

187. In the case of a component that is significant due to its individual financial significance within the group, the group audit team, or a component auditor on its behalf, should audit the financial information of the component using a component materiality value set by the group auditor. For a component that is significant due to its specific nature or circumstances and because it is likely to mean significant risks of material misstatement of the group financial statements, the group audit team, or a component auditor on its behalf, may not need to audit the financial information but may apply specified audit procedures relating to the significant risks identified. In the case of components that are not significant, the group audit team should perform analytical procedures at group level.

188. When developing or adopting auditing standards based on, or consistent with, the Fundamental Principles of Financial Auditing, it may be useful to consider the detailed guidance on group audits in ISSAI 1600\textsuperscript{24}.

\textsuperscript{24}ISSAI 1600 – Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors).
ISSAI 1000

General Introduction to
the INTOSAI Financial Audit Guidelines

International Standards of Supreme Audit Institutions, ISSAI, are issued by the
International Organization of Supreme Audit Institutions, INTOSAI. For more
information visit www.issai.org
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General Introduction to the INTOSAI Financial Audit Guidelines

Introduction

1. The INTOSAI Financial Audit Guidelines provide guidance for conducting financial audits of public sector entities.

2. The INTOSAI Financial Audit Guidelines represent the fourth level (Auditing Guidelines) of the International Standards of Supreme Audit Institutions (ISSAI) Framework, where the Founding Principles constitute the first level, the Principles and Guidelines for SAIs constitute the second level and the Fundamental Auditing Principles (the INTOSAI Auditing Standards) constitute the third level.\(^{25}\)

3. The INTOSAI Financial Audit Guidelines include the International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB). INTOSAI contributes to the development of those standards by participating in the IAASB Task Forces responsible for developing new standards or revising existing standards.

4. Practice Notes (PN), which are included in the INTOSAI Financial Audit Guidelines, provide relevant guidance on applying each ISA in financial audits of public sector entities in addition to that provided in the corresponding ISA.

5. In applying the INTOSAI Financial Audit Guidelines in financial audits of public sector entities, Supreme Audit Institutions recognize that the ISAs and the PNs together form the guidance. If referring in the auditor’s report to the fact that the audit was conducted in accordance with the ISSAIs, public sector auditors comply with all the ISSAIs relevant to the audit, as explained in the section on authority (paragraphs 28-43).

6. By comparison with the objectives of an audit of financial statements in accordance with the ISAs (i.e. to express an opinion whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework), the objectives of a financial audit of

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\(^{25}\) An illustration of the link between the INTOSAI Fundamental Auditing Principles (ISSAI 100–400) and the INTOSAI Financial Audit Guidelines (ISSAI 1000–2999) is available in appendix 1.
public sector entities may include additional audit and reporting responsibilities. For example, public sector auditors may be required to report on a public sector entity’s compliance or non-compliance with authorities, including budget and accountability; the effectiveness of internal control over financial reporting; or on the economy, efficiency and effectiveness of programs, projects and activities.

7. The audit mandate for a Supreme Audit Institution, or the obligations for public sector entities arising from legislation, regulation, ministerial directives, government policy requirements, or resolutions of the legislature, may also result in additional audit and reporting responsibilities for public sector auditors.

8. The INTOSAI Financial Audit Guidelines do not contain detailed guidance on audit and reporting responsibilities relating to compliance with authorities. Such guidance is contained in the Compliance Audit Guidelines. ISSAI 4200 provides guidance for compliance performed together with an audit of financial statements. They build upon INTOSAI’s Fundamental Auditing Principles and have been designed to assist public sector auditors having responsibilities related to compliance with authorities. ISSAI 4200 supplements, and should be read together with the Financial Audit Guidelines (ISSAI 1000-2999), when having such broader responsibilities.

9. The Financial Audit Guidelines, when applied together with the Compliance Audit Guidelines, are intended to provide public sector auditors with a comprehensive set of guidance for audits of financial statements in the public sector, when compliance with authorities is included in the objective.

The Purpose of the INTOSAI Financial Audit Guidelines

14. The main purpose of the INTOSAI Financial Audit Guidelines is to provide INTOSAI members with a comprehensive set of guidelines for the audit of financial statements of public sector entities. The INTOSAI Financial Audit Guidelines include PNs developed by INTOSAI in addition to the ISAs developed by the IAASB. They together form a guideline in the INTOSAI standards framework.

15. The INTOSAI Fundamental Principles provide the overriding principles for the performance of and reporting on audits carried out by Supreme Audit
Institutions. However, by utilizing the detail of the ISAs insofar as it is relevant to financial audits conducted by Supreme Audit Institutions, and by developing PNs that deal with special considerations for financial audits of public sector entities, INTOSAI provides a comprehensive set of Financial Audit Guidelines that can be drawn upon by all Supreme Audit Institutions in all institutional settings and audit environments.

16. The PNs provide a clear statement on applicability of the ISA to audits of public sector entities as well as supplementary guidance to public sector auditors on the ISAs. The PNs are addressed to public sector auditors which include, when relevant, other auditors doing financial audits of public sector entities. Where applicable, they also deal with general guidance on additional audit and reporting responsibilities of public sector auditors. There is a separate PN for each ISA. PNs are issued on an ongoing basis as and when the IAASB issues new or revises existing ISAs. The INTOSAI Financial Audit Guidelines apply to audits of financial statements as defined by ISSAI 1200 and address additional public sector audit considerations. The audit and reporting responsibilities of Supreme Audit Institutions related to financial audits may include additional aspects of regularity audits (as clarified in paragraph 19). In the public sector, audits of financial statements will often be combined with audits of compliance with authorities. ISSAI 4200 addresses such additional auditing and reporting responsibilities. Audits of compliance with authorities include the assessment of whether the activities, financial transactions and information are reflected or contained in the accounts or financial statements are in accordance with applicable resolutions of the legislature, including budgetary laws or decisions for such, provisions for funds, contracts, grant agreements etc.

17. The INTOSAI Financial Audit Guidelines apply to audits at all levels of government. Depending on the audit mandate or law governing the Supreme Audit Institution, the INTOSAI Financial Audit Guidelines may apply to audits of private sector entities when they are involved in the management of public services or public monies, for example through partnership arrangements or as recipients of public grants or subsidies.

26ISSAI 1200 “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards of Auditing.”
**Scope of the INTOSAI Financial Audit Guidelines**

18. The objective of the INTOSAI Financial Audit Guidelines is to provide guidance for audits of financial statements in the public sector, including general guidance on additional auditing and reporting objectives related to the public sector audit of financial statements.

19. The INTOSAI Fundamental Principles do not define an audit of financial statements. According to ISSAI 100\(^27\) the full scope of government auditing includes regularity and performance audit. Regularity audit embraces:

(a) Attestation of financial accountability of accountable entities, involving examination and evaluation of financial records and expression of opinions on financial statements;

(b) Attestation of financial accountability of the government administration as a whole;

(c) Audit of financial systems and transactions including an evaluation of compliance with applicable statutes and regulations;

(d) Audit of internal control and internal audit functions;

(e) Audit of the probity and propriety of administrative decisions taken within the audited entity; and

(f) Reporting of any other matters arising from or relating to the audit that the Supreme Audit Institutions considers should be disclosed.

20. The scope of a regularity audit performed in accordance with the ISSAI 100 is thus wider than the scope of an audit of financial statements conducted in accordance with the ISAs.

21. Furthermore, the definition of financial audit within each Supreme Audit Institutions depend on regulations, mandate and organizational structure. The mandate of a Supreme Audit Institution may specify auditing and reporting responsibilities different from, or in addition to the audit of financial statements. Such responsibilities may either be included in, or may be in addition to, the audit of financial statements. The audit of such information will require public sector auditors to perform work that is in addition to what is required solely for auditing and reporting on the financial statements in accordance with the ISAs.

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\(^{27}\) ISSAI 100- “INTOSAI Auditing Standards- Basic Principles”, paragraphs 38 and 39.
22. Due to INTOSAI’s involvement in the development of the ISAs, the ISAs include application material relevant to financial audits of public sector entities, often provided under a separate heading. The PNs provide additional guidance to be considered if relevant to the mandate of the Supreme Audit Institutions.

23. Although the Financial Audit Guidelines may provide guidance on audit and reporting responsibilities in addition to those in the ISAs, it is not their intent to provide guidance on the full scope of a regularity audit performed in accordance with the INTOSAI Fundamental Principles, or all the different or additional audit or reporting responsibilities of the mandates of Supreme Audit Institutions. For responsibilities other than audit of financial statements public sector auditors may need to apply other relevant INTOSAI guidelines. ISSAI 420028 provide guidance on audit responsibilities related to compliance audit as part of the audit of financial statements.

**Structure and Content of the INTOSAI Financial Audit Guidelines**

24. The INTOSAI Financial Audit Guidelines contain initially 38 ISSAIs. 36 of those include an ISA and in addition a Practice Note to support the adoption and use of the ISA in the public sector. The ISA and the PN together constitute one guideline on the subject matter at hand. The remaining ISSAIs, not based on or including an ISA, are ISSAI 1000, General Introduction to the INTOSAI Financial Audit Guidelines and ISSAI 1003, the Glossary29, which includes the IAASB Glossary and provides additional public sector terms and explanations.

25. The INTOSAI Financial Audit Guidelines are presented in the INTOSAI classification system as ISSAIs, starting with ISSAI 1000 to ISSAI 2999. The three last positions in the ISSAI number indicate the corresponding number of the ISA (for example, ISSAI 1800 includes ISA 800 and the Practice Note for ISA 800). Appendix 2 outlines the ISSAIs related to financial audit.

26. The ISAs have a structure, in which information is presented in separate sections:

(a) **Introduction**

Introductory material may include information regarding the purpose, the

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28 ISSAI 4200, “Compliance Audit Guidelines Related to Audit of Financial Statements.”
29 ISSAI 1003, “Glossary of Terms to the INTOSAI Financial Audit Guidelines.”
scope, and subject matter of the ISA, in addition to the responsibilities of the
auditors and others in the context in which the ISA is set.

(b) **Objective**

Each ISA contains a clear statement of the objective of the auditor in the
audit area addressed by that ISA.

(c) **Definitions**

For greater understanding of the ISAs, applicable terms have been defined in
each ISA.

(d) **Requirements**

The objective(s) is supported by clearly stated requirements. Requirements
are always expressed by the phrase “the auditor shall”. In applying the
INTOSAI Financial Audit Guidelines as guidance the word “shall” means
“may”. When reference to the ISAs is made in the Auditor’s Report, the
authority of the ISAs shall be followed.

(e) **Application and Other Explanatory Material**

The application and other explanatory material explains more precisely what
a requirement means or is intended to cover, or includes examples of
procedures that may be appropriate under given circumstances. The
application and other explanatory material may include sub-headings for
“specific considerations for public sector entities”. Such paragraphs have
been included as agreed with the IAASB to support the application in
financial audits of public sector entities. Some ISAs also contain
“considerations specific to audits of smaller entities”.

In audits of public sector entities and entities that receive government awards,
these considerations are usually not applicable, even if the public sector entity
has few employees, simple operations, or a relatively small budget. In those
situations, the public sector entity may still have complicated transactions, such
as transfers from other government entities, as well as a need to comply with
laws, regulations, policies and systems determined by a higher level of
government and a need for accountability for use of taxpayer monies.
Therefore public sector auditors carefully consider the relevance of such
considerations. The Practice Notes may include additional guidance in this area
when considered important to add guidance relevant for audits of smaller
public sector entities.
27. The Practice Notes to the ISAs are presented in separate sections:

(a) **Background**
Background material may include information regarding the ISA such as an introduction to the ISA, and the content of the Practice Note.

(b) **Applicability of the ISA in the Public Sector Auditing**
Each Practice Note contains a clear statement of applicability of the ISA for audits of public sector entities. Matters regarding the public sector auditor’s statutory responsibilities and the public sector auditor’s extended mandate (legality/regularity, compliance, and performance issues) may influence the applicability. In some PNs, when considered essential for the scope of the PN such references are included.

(c) **Additional Guidance on Public Sector Issues**
To assist public sector auditors in applying the ISA in audits of public sector entities, this section provides additional public sector specific guidance on a general level. It may be structured following the headings of the ISA. When relevant the paragraphs in this section have references to the related paragraphs of the ISA. The guidance may also contain examples more relevant to audits of public sector entities than provided for in the ISA. When relevant, additional applicable terms may also be defined in this section. The section is structured with subsections for each area. Examples of matters that are considered in this section include:

(i) Matters related to specific legislation applicable in the public sector;
(ii) Matters related to overarching public sector concerns, for example stewardship, accountability and transparency;
(iii) Matters related to different models of Supreme Audit Institutions (Auditor General and Court of Accounts models), and Supreme Audit Institutions that contract out work to external audit firms;
(iv) Matters related to accounting principles and practices particular to public sector entities;
(v) Matters related to particular government entities (ministries, agencies, quasi-govern-mental), and sectors (finance, defense, justice, health, environment, etc), if any;
(vi) Other matters related directly to the application of the ISA in financial audits of public sector entities.
Applying the INTOSAI Financial Audit Guidelines

28. Reference to the use of standards can be made in one of four ways depending on the standards applied and the SAI’s mandate:

(a) In accordance with the ISSAIs (1000-2999) which means full compliance with all relevant ISAs and the additional guidance set out in the INTOSAI Practice Notes to the ISAs.

(b) In accordance with the ISAs which means full compliance with all relevant ISAs.

(c) In accordance with the INTOSAI Fundamental Auditing Principles\(^{30}\), but not full compliance with the ISAs which are presently included as part of the INTOSAI Financial Audit Guidelines (ISSAIs 1000-2999)\(^{31}\).

(d) In accordance with other national and relevant Auditing Standards

29. Public sector auditors who state in their auditor’s report on a set of financial statements that the audit has been conducted in accordance with the ISAs are also encouraged to apply the additional public sector guidance in ISSAIs 1000-2999. Where public sector auditors have additional audit and reporting responsibilities, references to applicable standards will also be necessary.

Applying the INTOSAI Financial Audit Guidelines to Support INTOSAI Fundamental Principles

30. The INTOSAI Financial Audit Guidelines are developed to support the application of the INTOSAI Fundamental Principles\(^{32}\) as well as the ISAs (as standards or as guidance together with the Practice Notes). INTOSAI Fundamental Principles are written to provide general standards for all audit activities carried out by a Supreme Audit Institutions. Applying the INTOSAI Financial Audit Guidelines as guidance will not diminish the use of INTOSAI

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\(^{31}\) A new Fundamental Auditing Principles referred to in option c (ISSAI 1000/28) were withdrawn. In the years 2007 – 2013, the Fundamental Auditing Principles referred to the INTOSAI Auditing Standards. These were elaborated in 1992 and were included in the ISSAI Framework at level 3 – Fundamental Auditing Principles in 2007. In a transition period until 2016 reference set of Fundamental Auditing Principles was endorsed by INTOSAI in 2013. At the same time the to this set of standards may be made by stating “We conducted our audits in accordance with the INTOSAI Auditing Standards from 1992”. The standards are annexed to this ISSAI as appendix 6.

\(^{32}\) Ibid.
Fundamental Principles as the authoritative auditing standards. In this circumstance reference is made to the INTOSAI Fundamental Principles as the authoritative standards applied.

Applying the INTOSAI Financial Audit Guidelines to Support other Standards

31. The INTOSAI Financial Audit Guidelines may also, if relevant, be used by Supreme Audit Institutions to support the use of other national standards for financial audits. This is appropriate only when the national audit standards are consistent with the INTOSAI Financial Audit Guidelines.

Authority

Authority – INTOSAI Fundamental Principles and Financial Audit Guidelines

32. INTOSAI Fundamental Principles contains the fundamental auditing principles for audit work conducted by the Supreme Audit Institution. While it is the responsibility of each Supreme Audit Institution to judge the extent to which the standards are compatible with its mandate, viewed in the particular constitutional, legal and other circumstances of the audit organization, one of the principles outlined in the INTOSAI Code of Ethics is the public sector auditor’s obligation to apply generally accepted auditing standards.

33. The INTOSAI Fundamental Principles will remain the framework of audit standards for INTOSAI members, and the authority of those standards is in no way diminished by the publication of the INTOSAI Financial Audit Guidelines including the ISAs and the PNs. INTOSAI recognizes that this framework together with the guidance provided by the INTOSAI Financial Audit Guidelines will provide INTOSAI members with relevant concepts and guidance for conducting financial audits.

34. The Preface of the INTOSAI Fundamental Principles states that, although the word “standards” is used throughout the documents, it is understood that this word is to be used synonymously with the authority for compliance within the

\[33\] ISSAI 100- “INTOSAI Auditing Standards- Basic Principles”, ISSAI 200- “INTOSAI Auditing Standards-General Standards”, ISSAI 300- “INTOSAI Auditing Standards-General Standards”, and ISSAI 400- INTOSAI Auditing Standards- Reporting Standards”.

\[34\] ISSAI 30- “INTOSAI Code of Ethics”
domain of each Supreme Audit Institution. The foreword to the INTOSAI Fundamental Principles states that, while INTOSAI Auditing Standards do not have mandatory application, they reflect a “best practice” consensus among Supreme Audit Institutions and therefore each institution must judge the extent to which the standards are compatible with its mandate.

35. The INTOSAI Financial Audit Guidelines are to be considered with reference to the INTOSAI Fundamental Principles. As a result the INTOSAI Financial Audit Guidelines PNs do not stipulate requirements for application, and do not use the terms “shall” or “should”. The ISAs include such terms, and differentiate between requirements and application and other explanatory material. However, these should similarly not be regarded as mandatory for Supreme Audit Institution.

36. Auditors of public sector entities may use the INTOSAI Financial Audit Guidelines as comprehensive guidance for conducting financial audits. When the guidelines are used as standards, auditors of public sector entities respect the authority of the ISAs. Paragraphs 37-43 deal with the authority of the ISAs.

**Authority – International Standards on Auditing**

37. The objective of the IAASB is to serve the public interest by setting, independently and under its own authority, high-quality auditing, assurance, quality control and related services standards, and by facilitating the convergence of national and international standards, thereby enhancing the quality and uniformity of practice throughout the world and strengthening public confidence in the global auditing profession.

38. The IAASB develops ISAs, International Standards on Review Engagements (ISREs), Inter-national Standards on Assurance Engagements (ISAEs) and International Standards on Related Services (ISRSs). These Standards are collectively referred to as the IAASB’s Engagement Standards. The IAASB also develops International Standards on Quality Control (ISQC). The Engagement Standards and the ISQCs are collectively referred to as the International Standards. The INTOSAI Financial Audit Guidelines include the ISAs. They do not override the local laws or regulations that govern the audit of historical
39. According to the Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services, the ISAs are written in the context of an audit of financial statements by an independent auditor (unless otherwise stated in the ISAs, this means financial statements comprising historical financial information). The objective of an audit of financial statements is to enable the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework. The ISAs, taken together, provide the standards for the auditor’s work in fulfilling this objective.

40. As the ISAs issued by the IAASB are increasingly recognized by the international community as the international standards for audits of financial statements, they provide a strong basis for guidance on how to implement the INTOSAI Fundamental Principles.

41. Since 2003 INTOSAI has had a Memorandum of Understanding with the IAASB. Under the terms of the Memorandum of Understanding INTOSAI nominates experts drawn from the wider INTOSAI membership to participate in IAASB task Forces responsible for developing new or revising existing ISAs. Experts on IAASB Task Forces promote the inclusion of public sector considerations in the ISAs, thereby enhancing the application of the ISAs in financial audits of public sector entities. The nature of the International Standards requires the professional accountant to exercise professional judgment in applying them.

42. The scope, effective date and any specific limitation of the applicability of a specific ISA is made clear in the ISA. Unless otherwise stated in the ISA, the professional accountant is permitted to apply an ISA before the effective date specified therein.
43. If public sector auditors state in their auditors’ report on the financial statements that the audit has been conducted in accordance with the ISAs, they have to respect the authority attached to ISAs as set out in ISA 200 (Appendix 3).

**General Issues in Audits of Public Sector Entities**

44. This section deals with some general issues of public sector concern. It is not intended to cover all public sector issues that may be relevant to consider when conducting financial audits in a specific public sector environment. However, these issues have been regarded as having general importance for public sector auditors in applying the ISSAIs on financial audit.

45. Concepts outlined in paragraphs 46-88 relate to issues relevant to public sector auditors that are further explained in the individual PNs. However, the body of guidelines should be considered when applying the guidelines.

**Different Auditing Systems within the Public Sector**

46. Different external audit models exist around the world. The three most common systems are:

   (a) Auditor General model
   (b) Court of Accounts (or Audit) model
   (c) Board or Collegiate model.

47. However, every country may have a unique model and there are a great number of national variations in the way a Supreme Audit Institution operates, which may influence the way the ISSAIs may be adopted and implemented. The ISSAIs are developed to provide guidance for public sector auditors regardless of the system within which they operate. The Auditor General systems normally have a strong focus on financial audit and operate under such conditions that adopting the ISSAIs may be more relevant. The Board or Collegiate model is similar to the Auditor General model, except for the internal structure of the audit institution. A key difference in a Court of Accounts system is that in such a system government officials are normally held personally liable if unauthorized or illegal payments are made. However, similar sanctions may also apply for some Auditor General models. The Supreme Audit Institutions may in such
environments impose penalties or corrections on audited officials. The main focus of the audit work is often to verify the legality of transactions rather than providing an opinion on the true and fair view of the financial statements. A Board or Collegiate model may also have such judicial functions. INTOSAI Fundamental Principles\textsuperscript{35} states that because of the approach and structure of some Supreme Audit Institutions, not all INTOSAI auditing standards apply to all aspects of their work, for example, the judicial nature of the reviews conducted by Courts of Account make aspects of their work fundamentally different from the financial and performance audits conducted by Supreme Audit Institutions which are organized under a hierarchy system led by an Auditor-General or a Comptroller General. INTOSAI standards do not cover these jurisdictional powers in detail.

48. Specific guidance for Supreme Audit Institutions with a judicial role, such as a Court of Accounts model, has, when deemed necessary, been included in ISSAIs 1000-2999. The strong focus on compliance issues within such a system may introduce a need to adopt the INTOSAI Compliance Audit Guidelines\textsuperscript{36} as well as the INTOSAI Financial Audit Guidelines.

**Terminology Used in the Guidelines**

49. As part of the cooperation between INTOSAI and the IAASB “sector neutral” terminology is included in the ISAs when possible so that they can be readily understood and applied in both the public and private sectors. This has been done through including appropriate text in the standards themselves or in the related glossary. Additional definitions, introduced in the Practice Notes may also be found in the glossary to the INTOSAI Financial Audit Guidelines\textsuperscript{37}.

50. One example of a fundamental concept in the ISAs is that there are significant public interest issues related to the audits of “listed entities” (entities quoted on a recognized stock exchange). The ISAs set out several requirements related specifically to listed entities. Listed entities, as such, may not be common in the public sector. However, public sector entities that are significant due to size, complexity, or public interest aspects may have a wide range of stakeholders and

\textsuperscript{35} ISSAI 100 “INTOSAI Auditing Standards – Basic Principles”, paragraph 13
\textsuperscript{36} ISSAI 4000, ISSAI 4001 and ISSAI 4002
\textsuperscript{37} ISSAI 1003 “Glossary of Terms to the INTOSAI Financial Audit Guidelines”
may be comparable to listed entities. The Practice Notes deal with such concepts which may need to be interpreted in a different way in the public sector.

51. The use of typical private sector specific terms such as “firm” and “company” have been to some extent replaced with sector neutral terms in the ISAs to reflect the broader use. In some ISSAI, such as ISSAI 1315\textsuperscript{38}, references are made to terms used in the ISA such as business, marketing and sales personnel when describing the internal controls structure and components as well as the risk assessment process. Corresponding terms in the public sector are mandate, program objectives and program managers and other program staff.

**Professional Judgment and Skepticism**

52. The terms “professional judgment” and “professional skepticism”\textsuperscript{39} are frequently used in the ISAs when formulating requirements relating to the auditor’s decisions about the appropriate course of action and to express the attitude that includes a questioning mind. These concepts are not introduced in the INTOSAI Fundamental Principles. The INTOSAI Fundamental Principles\textsuperscript{40} address the concept of due care and state: “Auditors need to be alert for situations, control weaknesses, inadequacies in record keeping, errors and unusual transactions or results which could be indicative of fraud, improper or unlawful expenditure, unauthorized operations, waste, inefficiency or lack of probity.” The concept of professional skepticism enhances and broadens the concept of due care and is fundamental for planning and performance of the audit. These concepts are basic for most professional standards and are now introduced in the INTOSAI Financial Audit Guidelines.

**Engagement Acceptance and Continuance**

53. The ISAs require that in certain situations the auditor disclaims an opinion or withdraws (or resigns) from the engagement, where withdrawal is possible under applicable law or regulation. Withdrawal may be required, for example, when:

- the auditor and management cannot agree on the terms of the engagement;

\textsuperscript{38} ISSAI 1315—“Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment,”

\textsuperscript{39} See ISSAI 1003 – “Glossary of Terms to the INTOSAI Financial Audit Guidelines” , for complete definitions

\textsuperscript{40} ISSAI 200 – “INTOSAI Auditing Standards- General Standards”, paragraph. 2.41
• ethical requirements cannot be met;
• significant difficulties are encountered, such as the inability to access documents or perform required procedures;
• the auditor risks being associated with misleading information, and
• scope limitations prohibit them from obtaining sufficient, appropriate audit evidence on which to base their audit opinion.

Objective of an Audit of Financial Statements

55. The ISAs are written in the context of an auditor conducting an audit of financial statements in accordance with the ISAs whereas such audits may only be a part of the public sector audit task. ISA 200⁴¹ describes the framework within which ISAs are to be applied. The ISAs do not specifically deal with separate engagements for reporting on performance audits, compliance with laws and regulations, or matters such as inadequate systems of control. ISA 200 explains the overall objective of the auditor in conducting an audit of financial statements as being:

(a) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and

(b) To report on the financial statements, and communicate as required by the ISAs, in accordance with the auditor’s findings.

56. The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. In the case of most general purpose frameworks, that opinion is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view in accordance with the framework. Laws or regulations for public sector audit organizations may prescribe the use of other wordings for expressing

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⁴¹ ISA 200 – “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With International Standards on Auditing”
the opinion. An audit conducted in accordance with ISAs and relevant ethical requirements enables the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an identified financial reporting framework.

57. The Lima Declaration⁴² states “Audit is not an end in itself but an indispensable part of a regulatory system whose aim is to reveal deviations from accepted standards and violations of the principles of legality, efficiency, effectiveness and economy of financial management early enough to make it possible to take corrective action in individual cases, to make those accountable accept responsibility, to obtain compensation, or to take steps to prevent – or at least render more difficult – such breaches.” This is a much broader task than providing an opinion on financial statements. These broader overall audit objectives may be addressed in other parts of INTOSAI’s Framework for Professional Standards. The INTOSAI Financial Audit Guidelines are relevant to financial audits of public sector entities. The often broader responsibilities may result in a need to apply other ISSAIs for additional responsibilities.

58. The INTOSAI Fundamental Principles stipulate⁴³ (ISSAI 100) that for some elements of the Supreme Audit Institution’s mandate, particularly in regard to the audit of financial statements, the Supreme Audit Institution’s audit objectives may be similar to the objectives of audits in the private sector. ISSAI 300⁴⁴ states that the auditor should design audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, and illegal acts that could have a direct and material effect on the financial statement amounts or the results of regularity audits. Regularity requirements in the public sector are rarely less important in public accountability than expressing an opinion on the financial statements within broad materiality allowances. The objective of ISAs are to enable the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an identified financial reporting frame-work. A Supreme Audit Institution’s objective of auditing is thus wider than the objectives of an audit according to the ISAs. Furthermore,

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⁴²ISSAI 1 – “The Lima Declaration”
⁴³ISSAI 100 – “INTOSAI Auditing Standards – Basic Principles”
⁴⁴ISSAI 300 – “INTOSAI Auditing Standards – General Standards”
the user of a financial statement audit report in the public sector looks at more extensive accountabilities than those implied by ISA 200 (‘the economic decisions of users’). The INTOSAI Financial Audit Guidelines together with other INTOSAI standards and guidelines will together serve the wider objective of public sector auditing.

Agreeing the Terms of Audit Engagements

59. The ISAs generally deal with tasks that are undertaken through agreement with clients. Supreme Audit Institutions normally undertake assignments intended to provide reports on accountabilities to legislative or governing bodies. These assignments are usually mandated by legislation and the Supreme Audit Institution is required to carry out the assigned functions. In some public sector environments there may in addition to mandated responsibilities be contractual measures for audit tasks.

60. ISA 210 deals with the terms of an engagement and provides requirements on the auditors in relation to acceptance of an assignment. These requirements illustrate the reliance of the ISAs on a client relationship rather than the legislated powers of the Supreme Audit Institutions. Nevertheless the need for a cooperative relationship with the audited entity is common to both.

61. In addition to the requirements and guidance set out in the ISAs, there may be further considerations for public sector auditors in undertaking audit engagements. For example, the capabilities and competence required in an audit may be broader and include the need to understand applicable reporting arrangements, such as requirements for reporting to the legislature, governing body, or the public. Public sector auditors may sometimes need to adapt their approach in order to promote compliance with the requirements of the ISAs. They may do this, for example, by performing procedures such as those related to client acceptance and continuance to obtain valuable information for assessing risk and carrying out reporting responsibilities.

62. Supreme Audit Institutions are normally required to carry out an audit as stated in their mandate. They do not normally have the option to reject an assignment. ISA 210 includes requirements on the auditor not to accept an engagement if

45ISA 210 – “Agreeing The Terms of Audit Engagements”
certain circumstances are not met, unless required to do so by law or regulation. In such cases, when the requirement is not applicable, the Practice Note will provide additional guidance on suitable actions for public sector auditors.

63. ISA 210 requires the auditor to obtain the agreement of management and, where appropriate, those charged with governance that they acknowledge and understand their responsibility. If law or regulation prescribes in sufficient detail the terms of the engagement, it may not be necessary to record them in an audit engagement letter or other suitable form of written agreement. An exception may be for the agreement by management and, where appropriate, those charged with governance, that they acknowledge and understand the responsibilities set out in the ISA. Such engagements often exist in the public sector and written agreements on the terms of engagements are not often used. The INTOSAI Financial Audit Guidelines support introducing such agreements in public sector auditing for reasons set out in the Practice Note.

Quality Assurance Processes

64. The INTOSAI Fundamental Principles do not contain a separate standard on quality control for audit work, but some guidance is contained in the general standards. These do not clearly state the individual auditor’s responsibilities for quality control, but instead focus on the Supreme Audit Institution’s responsibility to establish quality assurance arrangements. ISA 220 requires the auditor to implement quality control procedures on individual audits. The provisions of ISA 220 are applicable to the work of Supreme Audit Institutions. This ISA is premised on the basis that the firm (or the public sector equivalent) is subject to quality control procedures according to ISQC1 or national requirements that are at least as demanding.

65. In private sector audit firms, engagement partners generally have individual responsibility for audit engagements and also have the authority to bind the audit firm. For Supreme Audit Institutions, an Auditor General, a Board or a Court of Accounts has overall responsibility, although the day-to-day operational

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46ISSAI 200, “INTOSAI Auditing Standards - General Standards”, paragraph 1.27
47ISA 220, “Quality Control for an Audit of Financial Statements.”
48ISQC 1, “Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and other Assurance related Service Engagements.”
responsibility may be delegated to others. For example, all those with engagement partner responsibility in a Supreme Audit Institution with an Auditor General System would, because of the hierarchical structure ultimately report to the Auditor General. In the public sector, it is important to select engagement quality control reviewers who are independent of the audited entity and can provide an objective evaluation even though they are part of the same strategic leadership as the person with engagement partner responsibility.

66. Furthermore, ISQC 1\(^4\) requires engagement partner rotation for listed entities after a predefined period. In the public sector, this requirement may be applied to significant public interest entities. However, legislation establishing the appointments and terms of office of the Auditor General may make rotation impractical. Supreme Audit Institutions may establish policies and procedures to promote compliance with the spirit of this requirement (e.g., by rotating key personnel with operational responsibility for the audit engagement, requiring engagement quality control reviews, or carrying out regular peer reviews).

**Working Papers and Audit Documentation**

67. The INTOSAI Fundamental Principles\(^5\) state that the auditor should ensure that working papers contain evidence adequately supporting all conclusions, recommendations and opinions. Furthermore paragraph 5.5 requires that auditors should adequately document the audit evidence in working papers, including the basis and extent of the planning, work performed and the findings of the audit. ISA 230\(^6\) requires the auditor to assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor’s report. It also requires the auditor not to delete or discard audit documentation of any nature before the end of its retention period. ISQC1\(^7\) (or national requirements that are at least as demanding) requires audit organizations to establish policies and procedures for

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\(^4\)ISQC 1 – “International Standard on Quality Control 1- Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Service Engagements”. This standard establishes requirements on audit firms related to quality controls, and is not included in the INTOSAI Financial Audit Guidelines.

\(^5\)ISSAI 300 – “INTOSAI Auditing Standards- Field Standards”, paragraph 2.3 (d)

\(^6\)ISA 230 – “Audit Documentation”

\(^7\)ISQC 1 – “International Standard on Quality Control 1- Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Service Engagements”.
the timely completion of the assembly of audit files. In the public sector such requirements for documentation and retention may be governed by legislative requirements related to confidentiality on the one hand, and access by third parties on the other hand. ISQC 1 establishes requirements on audit firms (and public sector equivalents) related to quality controls. The Practice Note to ISA 230 provides additional guidance related to documentation.

**Communication**

68. ISA 260\(^3\) defines those charged with governance as “the person(s) or organization(s) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity.” In the public sector, identifying those charged with governance may be a challenge. The audited entity may be part of a larger or broader structure with governance bodies at several organizational levels. In some cases, there may also be separate reporting requirements related to aspects of financial and compliance audits involving separate governance bodies. The Practice Notes to the ISAs dealing with communication provide appropriate guidance to meet the needs and expectations of the legislature or appropriate regulators.

69. ISA 260 sets out requirements for annual communication of compliance with ethical requirements regarding auditor’s independence. In addition to the considerations described in the ISSAI, matters set out in the INTOSAI Code of Ethics, such as political neutrality, may also be important for public sector auditors.

70. Public sector auditors may also have broader communication responsibilities than those envisioned by ISA 260. As stated in relevant Practice Notes, public sector auditors may have such responsibilities to communicate with the legislature, appropriate regulators, or relevant funding agencies.

**Identifying Fraud and Error**

71. The INTOSAI Fundamental Principles\(^4\) states that the Supreme Audit Institution should ensure that the techniques employed are sufficient to reasonably detect all

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\(^3\)ISA 260 – “Communication With Those Charged With Governance”

\(^4\)ISSAI 300 – “INTOSAI Auditing Standards- Field Standards” paragraph 5.3.
quantitatively material errors and irregularities. ISA 240\textsuperscript{55} requires, as a basic principle, that the auditor shall, when planning the audit, assess the risk that fraud or error may cause the financial statements to contain material misstatements. It also requires the auditor to inquire of management as to any fraud which has been discovered. Public sector auditors may have formally mandated responsibility to detect fraud, and in addition, the use of public monies tends to impose a higher profile on fraud issues. As a result auditors may need to be responsive to public expectations regarding detection of fraud.

72. Another area that may include significant differences compared to private sector audits is related to public sector auditor’s responsibilities, in some public sector environments, for actions to be taken when offences are discovered. The Practice Note to ISA 240 makes reference to the possible extended reporting responsibilities within the public sector, to address concerns about public accountability.

73. Many Supreme Audit Institutions are responsible for contributing to the prevention and detection of fraud in line with the INTOSAI Fundamental Principles. ISA 240 expands on the audit risk standards and deals with their application in relation to the risk of material misstatement due to fraud. In the public sector, auditors’ responsibilities may result from legislation, regulation, or directives related to the audited entity or may be covered separately by the audit mandate. As a result, those responsibilities may not be limited to the risk of material misstatement of the financial statements due to fraud. The auditor’s responsibilities related to fraud may be broader than in the private sector and may include aspects of compliance, public accountability, and sound public sector financial management.

74. Areas where public sector auditors are alert to fraud risks are included in the related Practice Note and include areas such as procurement, grants, privatizations, intentional misrepresentation of results or information, and misuse of authority or power.

**The Auditor’s Consideration of Laws and Regulations**

75. ISSAI 300\textsuperscript{56} states that the regularity audit is an essential aspect of government

\textsuperscript{55}ISA 240 – “The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements”
\textsuperscript{56}ISSAI 300- “INTOSAI Auditing Standards- Field Standards” paragraph 4.
auditing. One important objective of this type of audit is to make sure, by all means possible, that the State budget and accounts are complete and valid. This will provide Parliament and other users of the audit report with assurance about the size and development of the financial obligations of the State. To achieve this objective, public sector auditors may examine the accounts and financial statements of the administration with a view to assuring that all operations have been correctly undertaken, completed, paid and accounted for. The INTOSAI Fundamental Principles focus on the importance of reviewing compliance with laws and regulations when auditing in the public sector because decision makers need to know if the laws and regulations are being followed, whether they are having the desired results, and, if not, what revisions are necessary. In addition to the audit of financial statements, many public sector engagements include additional audit responsibilities with respect to the consideration of laws and regulations which have no material effect on the financial statements. ISSAI 4200 addresses auditor responsibilities related to an audit of compliance in relation to an audit of financial statements.

76. ISA 250 states that the auditor is not responsible for preventing non-compliance with law and regulations. Public sector auditors may have, as stated above, additional responsibilities related to compliance with law and regulations. In addition, public expectations may be considered when planning and performing audit procedures.

Risk Assessment and Audit Procedures

77. The audit risk standards are fundamental in risk-based audit approach. These standards normally refer to business risk, which ISA 315 defines as a “risk resulting from significant conditions, events, circumstances, actions or inactions that could adversely affect an entity’s ability to achieve its objectives and execute its strategies, or from the setting of inappropriate objectives and

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57 ISSAI 300 – “INTOSAI Auditing Standards- Field Standards” paragraph 4.2
58 ISSAI 4200 – Compliance Audit Related to the Audit of Financial Statements
59 ISA 250 – “Consideration of Laws and Regulations in an Audit of Financial Statements
60 ISA 315 – “Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment”, ISA 330- “The Auditor’s Responses to Assessed Risks” and ISA 500- “Audit Evidence”
strategies. “Business risk is broader than the risk of material misstatement on financial statements.

78. The business risk general concept applies in the context of identifying and assessing risk in public sector audit work. In the public sector, business risk relates to the risk that government activities, including relevant programs, program strategies, and objectives, will not be completed or achieved. In addition, risks related to issues such as the political climate, public interest, and program sensitivity or potential non-compliance with legislation or proper authority are relevant in the public sector context.

79. In addition to the requirements and guidance set out in the risk ISAs, there may be further considerations for public sector auditors in assessing risk and designing audit procedures. To gain an understanding of the entity, public sector auditors consider their broader mandate as well as any relevant legislation, regulations, directives, or other requirements that affect the entity’s operations. Management objectives, including public accountability concerns, are also considered. Risk assessment information may also be obtained from performance auditors or other relevant sources, such as testimonies from government officials or legislative reports or minutes.

80. Public sector auditors may have reporting responsibilities, such as those related to effectiveness of internal control or compliance with laws and regulations, which private sector auditors do not have. Consequently, public sector auditors’ reviews of internal controls may be broader and more detailed than in the private sector. Reporting requirements may also be broader in that public sector auditors may be required to communicate all identified internal control deficiencies or compliance deviations (not only those that are material) to the legislature or other governing body. Guidance on risk assessment issues is provided for in the relevant Practice Notes.

Materiality in Audits of Public Sector Entities

81. The risk of material misstatements is defined in ISA 200 as: “The risk that the
financial statements are materially misstated prior to audit”. In a financial statement audit, a misstatement is material, individually or when aggregated with other misstatements, when it could reasonably be expected to influence the economic decisions users take based on the financial statements. Materiality has both quantitative and qualitative aspects. In the public sector, materiality may not be limited to economic decisions of users. Legislators and regulators are often the primary users of public sector financial statements. They may use the financial statements to make not only economic decisions but also decisions about whether to continue certain government programs or grant funding. The qualitative aspects of materiality generally play a greater role in the public sector than in the private sector.

82. The ISAs dealing with materiality set out procedures for determining levels of materiality. In the public sector, materiality levels may be determined at a lower level than those prescribed by the ISAs due to considerations such as the sensitive nature of certain transactions or programs, the public interest, the need for effective legislative oversight and regulation, and the nature of the misstatement or deviation (e.g., if it is related to fraud or corruption).

83. The broader mandate in the public sector may require audits of certain aspects related to compliance and internal control. While misstatements of small monetary amounts may be deemed trivial, even small deviations related to compliance or internal control are, by their nature, generally not seen as trivial. Even if a transaction – regardless of size – is correctly recorded in the financial statements, the transaction represents an instance of non-compliance or a control deviation if it is illegal or fraudulent or if the control was not followed.

84. Many public sector auditors have a responsibility to report all (not only non-trivial) identified misstatements or compliance and control deviations to management or those charged with governance. Such misstatements or deviations may also have implications in a broader context. Based on their mandates, some Supreme Audit Institutions may also order that any instances of non-compliance be corrected.

**Auditor’s Reports in the Public Sector**

85. Greater consistency in the form of audit reports promotes credibility, as the
report can be readily identified as being prepared based on professional standards. It also helps readers to more easily identify any modifications of the Auditor’s opinion and audit findings such as internal control deficiencies and instances of non-compliance with authorities. ISA 700, 705, 706, 800, 805, and 810 discuss the form of the auditor’s report required for audits performed in accordance with the ISAs. In the private sector, the audit report is generally a one-way communication addressed to the appropriate parties, such as the shareholders or the board of directors. It identifies the audit work performed and the standards on which the work was based. The responsibilities of the auditor and management are set out and the auditor’s opinion is clearly stated. In certain circumstances, the report may also include additional paragraphs that further elaborate on important matters.

86. The same structure is normally relevant to public sector audit reports even though they tend to be longer and include a wider range of matters. In the public sector laws, the audit mandate or common practice may lead the public sector auditor to report findings, conclusions, recommendations and management responses. Such reporting is supplementary to the auditor’s report on the financial statements in accordance with ISSAI 1700.62.
Appendix 1 – Link between the INTOSAI Fundamental Auditing Principles (ISSAI 100-400) and the INTOSAI Financial Audit Guidelines (ISSAI 1000-2999)

1. This appendix is provided to reflect the interrelation between the INTOSAI Fundamental Auditing Principles and the International Standards of Auditing as included in the INTOSAI Financial Audit Guidelines together with a Practice Note. The link is presented with the starting point in the INTOSAI Fundamental Auditing principles. To each relevant topic or paragraph, in the Fundamental Principles, where further guidance could be found in an ISSAI included in the Financial Audit Guidelines, the related ISA is presented with number and title and a short description of the context.

2. This list is not intended to be a complete list of all the paragraphs of the INTOSAI Fundamental Principles and the related ISSAIs. It is provided to present an overview of how the financial audit guidelines and the ISAs fit into the INTOSAI structure.

ISSAI 100 – Basic Principles in Government Auditing

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# ISSAI 200 – General Standards in Government Auditing and Standards with Ethical Significance

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## Standards with Ethical Significance

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**Related guidance in ISSAI 1000-2999**

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Appendix 3 – The Authority Attached to the ISAs

An Audit of Financial Statements

3. The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. In the case of most general purpose frameworks, that opinion is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view in accordance with the framework. An audit conducted in accordance with ISAs and relevant ethical requirements enables the auditor to form that opinion. (Ref: Para. A1)

4. The financial statements subject to audit are those of the entity, prepared by management of the entity with oversight from those charged with governance. ISAs do not impose responsibilities on management or those charged with governance and do not override laws and regulations that govern their responsibilities. However, an audit in accordance with ISAs is conducted on the premise that management and, where appropriate, those charged with governance have acknowledged certain responsibilities that are fundamental to the conduct of the audit. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities. (Ref: Para. A2-A11)

5. As the basis for the auditor’s opinion, ISAs require the auditor to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. Reasonable assurance is a high level of assurance. It is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (that is, the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level. However, reasonable assurance is not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor’s opinion being persuasive rather than conclusive. (Ref: Para. A28–A52)
6. The concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements. In general, misstatements, including omissions, are considered to be material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. Judgments about materiality are made in the light of surrounding circumstances, and are affected by the auditor’s perception of the financial information needs of users of the financial statements, and by the size or nature of a misstatement, or a combination of both. The auditor’s opinion deals with the financial statements as a whole and therefore the auditor is not responsible for the detection of misstatements that are not material to the financial statements as a whole.

7. The ISAs contain objectives, requirements and application and other explanatory material that are designed to support the auditor in obtaining reasonable assurance. The ISAs require that the auditor exercise professional judgment and maintain professional skepticism throughout the planning and performance of the audit and, among other things:

- Identify and assess risks of material misstatement, whether due to fraud or error, based on an understanding of the entity and its environment, including the entity’s internal control.
- Obtain sufficient appropriate audit evidence about whether material misstatements exist, through designing and implementing appropriate responses to the assessed risks.
- Form an opinion on the financial statements based on conclusions drawn from the audit evidence obtained.

8. The form of opinion expressed by the auditor will depend upon the applicable financial reporting framework and any applicable law or regulation. (Ref: Para. A12-A13)

9. The auditor may also have certain other communication and reporting responsibilities to users, management, those charged with governance, or parties outside the entity, in relation to matters arising from the audit. These may be established by the ISAs or by applicable law or regulation.

63ISA 320, “Materiality in Planning and Performing an Audit” and ISA 450, “Evaluation of Misstatements Identified during the Audit.”
Overall Objectives of the Auditor

11. In conducting an audit of financial statements, the overall objectives of the auditor are:

a) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and

b) To report on the financial statements, and communicate as required by the ISAs, in accordance with the auditor’s findings.

12. In all cases when reasonable assurance cannot be obtained and a qualified opinion in the auditor’s report is insufficient in the circumstances for purposes of reporting to the intended users of the financial statements, the ISAs require that the auditor disclaim an opinion or withdraw (or resign)\(^\text{65}\) from the engagement, where withdrawal is possible under applicable law or regulation.

Definitions

13. For purposes of the ISAs, the following terms have the meanings attributed below:

(a) Applicable financial reporting framework – The financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation of the financial statements that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation.

The term “fair presentation framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:

(i) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or

(ii) Acknowledges explicitly that it may be necessary for management to

\(^{64}\)See, for example, ISA 260, “Communication with Those Charged with Governance;” and paragraph 43 of ISA 240, “The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements.”

\(^{65}\)In the ISAs, only the term “withdrawal” is used.
depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term “compliance framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (i) or (ii) above.

(b) Audit evidence – Information used by the auditor in arriving at the conclusions on which the auditor’s opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information. For purposes of the ISAs:

(i) Sufficiency of audit evidence is the measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor’s assessment of the risks of material misstatement and also by the quality of such audit evidence.

(ii) Appropriateness of audit evidence is the measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor’s opinion is based.

(c) Audit risk – The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.

(d) Auditor – “Auditor” is used to refer to the person or persons conducting the audit, usually the engagement partner or other members of the engagement team, or, as applicable, the firm. Where an ISA expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term “engagement partner” rather than “auditor” is used. “Engagement partner” and “firm” are to be read as referring to their public sector equivalents where relevant.

(e) Detection risk – The risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

(f) Financial statements – A structured representation of historical financial information, including related notes, intended to communicate an entity’s
economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information. The term “financial statements” ordinarily refers to a complete set of financial statements as determined by the requirements of the applicable financial reporting framework, but can also refer to a single financial statement.

(g) Historical financial information – Information expressed in financial terms in relation to a particular entity, derived primarily from that entity’s accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.

(h) Management– The person(s) with executive responsibility for the conduct of the entity’s operations. For some entities in some jurisdictions, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager.

(i) Misstatement – A difference between the amount, classification, presentation, or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework. Misstatements can arise from error or fraud. Where the auditor expresses an opinion on whether the financial statements are presented fairly, in all material respects, or give a true and fair view, misstatements also include those adjustments of amounts, classifications, presentation, or disclosures that, in the auditor’s judgment, are necessary for the financial statements to be presented fairly, in all material respects, or to give a true and fair view.

(j) Premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit is conducted – That management and, where appropriate, those charged with governance have acknowledged and understand that they have the following responsibilities that are fundamental to the conduct of an audit in accordance with ISAs. That is responsibility:

(i) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation;
(ii) For such internal control as management and, where appropriate, those charged with governance determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and

(iii) To provide the auditor with:
   a. Access to all information of which management and, where appropriate, those charged with governance are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
   b. Additional information that the auditor may request from management and, where appropriate, those charged with governance for the purpose of the audit; and
   c. Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

In the case of a fair presentation framework, (i) above may be restated as “for the preparation and fair presentation of the financial statements in accordance with the financial reporting framework,” or “for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework.” The “premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit is conducted” may also be referred to as the “premise.”

(k) Professional judgment – The application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.

(l) Professional skepticism – An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.

(m) Reasonable assurance – In the context of an audit of financial statements, a high, but not absolute, level of assurance.

(n) Risk of material misstatement – The risk that the financial statements are materially misstated prior to audit. This consists of two components, described as follows at the assertion level:

*Inherent risk* – The susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.

*Control risk* – The risk that a misstatement that could occur in an
assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity’s internal control.

(o) Those charged with governance – The person(s) or organization(s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

Requirements

Ethical Requirements Relating to an Audit of Financial Statements

14. The auditor shall comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements. (Ref: Para. A14-A17)

Professional Skepticism

15. The auditor shall plan and perform an audit with professional skepticism recognizing that circumstances may exist that causes the financial statements to be materially misstated. (Ref: Para. A18-A22)

Professional Judgment

16. The auditor shall exercise professional judgment in planning and performing an audit of financial statements. (Ref: Para. A23-A27)

Sufficient Appropriate Audit Evidence and Audit Risk

17. To obtain reasonable assurance, the auditor shall obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level and thereby enable the auditor to draw reasonable conclusions on which to base the auditor’s opinion. (Ref: Para. A28-A52)

Conduct of an Audit in Accordance with ISAs

Complying with ISAs Relevant to the Audit

18. The auditor shall comply with all ISAs relevant to the audit. An ISA is relevant to the audit when the ISA is in effect and the circumstances addressed by the ISA exist. (Ref: Para. A53-A57)
19. The auditor shall have an understanding of the entire text of an ISA, including its application and other explanatory material, to understand its objectives and to apply its requirements properly. (Ref: Para. A58-A66)

20. The auditor shall not represent compliance with ISAs in the auditor’s report unless the auditor has complied with the requirements of this ISA and all other ISAs relevant to the audit.

Objectives Stated in Individual ISAs

21. To achieve the overall objectives of the auditor, the auditor shall use the objectives stated in relevant ISAs in planning and performing the audit, having regard to the interrelationships among the ISAs, to: (Ref: Para. A67-A69)

(a) Determine whether any audit procedures in addition to those required by the ISAs are necessary in pursuance of the objectives stated in the ISAs; and (Ref: Para. A70)

(b) Evaluate whether sufficient appropriate audit evidence has been obtained. (Ref: Para. A71)

Complying with Relevant Requirements

22. Subject to paragraph 23, the auditor shall comply with each requirement of an ISA unless, in the circumstances of the audit:

(a) The entire ISA is not relevant; or

(b) The requirement is not relevant because it is conditional and the condition does not exist. (Ref: Para. A72-A73)

23. In exceptional circumstances, the auditor may judge it necessary to depart from a relevant requirement in an ISA. In such circumstances, the auditor shall perform alternative audit procedures to achieve the aim of that requirement. The need for the auditor to depart from a relevant requirement is expected to arise only where the requirement is for a specific procedure to be performed and, in the specific circumstances of the audit, that procedure would be ineffective in achieving the aim of the requirement. (Ref: Para. A74)

Failure to Achieve an Objective

24. If an objective in a relevant ISA cannot be achieved, the auditor shall evaluate
whether this prevents the auditor from achieving the overall objectives of the
auditor and thereby requires the auditor, in accordance with the ISAs, to modify
the auditor’s opinion or withdraw from the engagement (where withdrawal is
possible under applicable law or regulation). Failure to achieve an objective
represents a significant matter requiring documentation in accordance with ISA
230. (Ref: Para. A75-A76)
The International Standards of Supreme Audit Institutions, ISSAI, are issued by the International Organization of Supreme Audit Institutions, INTOSAI. For more information visit www.issai.org.
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Glossary of Terms to the INTOSAI Financial Audit Guidelines

Introduction

1. The INTOSAI Financial Audit Guidelines provide guidance for financial audit in the public sector.

2. The INTOSAI Financial Audit Guidelines represent the fourth level (Auditing Guidelines) of the International Standards of Supreme Audit Institutions (ISSAI) Framework, where the Founding Principles constitute level 1, the Codes for Supreme Audit Institutions the second level and the Fundamental Auditing Principles the third level (including the INTOSAI Auditing Standards).

3. The INTOSAI Financial Audit Guidelines draw, as far as possible, on the International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB). INTOSAI contributes to the development of those standards by participating in the IAASB Task Forces responsible for developing new standards or revising existing standards.

4. As part of the cooperation between INTOSAI and the IAASB, “sector neutral” terminology is included in the ISAs when possible, so that they can be readily understood and applied in both the public and the private sectors. This has been done through including appropriate text in the standards themselves or in the related glossary. Additional definitions, introduced in the Practice.

Notes may also be found in the glossary below.

5. Practice Notes (PN), which are included in the INTOSAI Financial Audit Guidelines, explain how to apply each ISA in a financial audit in the public sector. They also contain guidance relevant to financial audits in the public sector in addition to that provided in the corresponding ISA.

The Practice Note together with the related ISA constitutes a guideline within the ISSAI structure of standards.
6. In applying the INTOSAI Financial Audit Guidelines in financial audits in the public sector, Supreme Audit Institutions recognize that the ISAs and the PNs together form the guidance. If the reference in the auditor’s report state that the audit was conducted in accordance with the ISAs, public sector auditors comply with all the ISAs relevant to the audit.

Glossary of terms to the INTOSAI Financial Audit Guidelines

Abuse– Behavior that is deficient or improper when compared with behavior that a prudent person would consider reasonable and necessary business practice given the facts and circumstances. Abuse also includes misuse of authority or position for personal financial interests or those of an immediate or close family member or business associate. Abuse does not necessarily involve fraud, violation of laws, regulations, or provisions of a contract or grant agreement. Abuse is a departure from the concept of propriety, which relates to the general principles of sound public sector financial management and conduct of public sector officials.

Accountability– The principle those individuals, organizations and the community are responsible for their use of public resources and may be required to explain the use of public resources to others.

Agency – A type of government or parliamentary organization.

Appropriation of funds – An authorization granted by a legislative body to allocate funds for purposes specified by the legislature or similar authority.

Audit mandate – The auditing authority, responsibilities, discretions and duties conferred on a Supreme Audit Institution under the constitution or other lawful authority of a state.

Audit objective – In a financial audit of a private sector entity, the audit objective is limited to expressing an assurance opinion on a set of assertions. The objectives of a financial audit in the public sector, however, are often broader than expressing an opinion on whether the financial statements have been prepared, in all material respects, in accordance with the applicable financial reporting framework (i.e., the scope of the ISAs). The audit mandate, or obligations for public sector entities, arising from legislation, regulation, ministerial directives, government policy requirements, or resolutions of the legislature may result in additional objectives.

66The IFAC Glossary of Terms is used for audits performed in accordance with the ISAs. This Glossary of Terms provides additional definitions applicable to the public sector.
These responsibilities may include, for example, performing procedures and reporting instances of non-compliance with authorities, and the effectiveness of internal controls. However, even where there are no such additional objectives, there may be general public expectations in this regard.

Auditor General – The head of a Supreme Audit Institution constituted under the Auditor General Model.

Auditor General model – (See Audit General)

Authorities – Relevant acts or resolutions of the legislature or other statutory instruments, directions and guidance issued by public sector bodies with powers provided for in statute, with which the audited entity is expected to comply. (See also ISSAI 420067.)

Board or Collegiate model – Under the Board or Collegiate system, the Supreme Audit Institution has a number of members who form its college or governing board and take decisions jointly. Collegiate audit bodies normally are part of a parliamentary system of accountability. Reports and opinions agreed by the college are submitted to Parliament, where there is usually some form of Public Accounts Committee to act on them. Collegiate bodies may also have judicial functions. Broader mandate – (See Audit objective)

Business risk – Refers to the risk that activities – including relevant programs, program strategies, and objectives – will not be completed or achieved. In addition, risks related to issues such as the political climate, public interest, and program sensitivity or potential noncompliance with legislation or proper authority are relevant in the public sector context. (See also IFAC Glossary of Terms).

Compliance audit – Compliance audit deals with the degree to which the audited entity follows rules, laws and regulation, policies, established codes, or agreed upon terms and conditions etc. Compliance auditing may cover a wide range of subject matters. In general, the purpose of a compliance audit is to provide assurance to intended users about the outcome of the evaluation or measurement of a subject matter against suitable criteria.

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67 ISSAI 4200, “INTOSAI Compliance Audit Guidelines – Compliance Audit Related to the Audit of Financial Statements”
In performing compliance audits in the context of the INTOSAI Fundamental Auditing Principles, there are two concepts of significant relevance:

(a) **Regularity** - the concept that activities, transactions and information which are reflected in the financial statements of an audited entity are in accordance with authorizing legislation, regulations issued under governing legislation and other relevant, laws, regulations and agreements, including budgetary laws and are properly sanctioned; and

(b) **Propriety** - general principles of sound public sector financial management and conduct of public sector officials.

Depending of the mandate of the Supreme Audit Institution, a compliance audit may be an audit of regularity, or propriety, or both.

Because propriety is not readily susceptible to objective verification, it may be difficult, and in some cases impossible to audit propriety to a level of reasonable assurance. There are often no clear and objective benchmarks against which to measure propriety – what may be acceptable in one part of the public sector may not be acceptable elsewhere.

**Compliance Audit Guidelines** – The INTOSAI Compliance Audit Guidelines comprise:

(a) ISSAI 4000 “A general introduction to guidelines on compliance audit”;
(b) ISSAI 4100 “Compliance audit guidelines for audits performed separately from the audit of financial statements”; and
(c) ISSAI 4200 “Compliance audit guidelines related to the audit of financial statements”.

**Comptroller General** – The role of Auditor General may be combined with that of Comptroller. The Comptroller function is one of control rather than audit and is performed in advance of expenditure being incurred.

**Court of Accounts** – In a Court of Accounts model the Supreme Audit Institution is an integral part of the judicial system operating independently of the executive and legislative branches. It is likely to have only a limited relationship with the national Parliament. The Supreme Audit Institution is normally known as the Court of Accounts (or Court of Audit) and is generally a self standing Court dealing only with financial matters. Less commonly, it may be part of the Supreme Court, and is then normally known as a Chamber of Accounts.
Some key features are:

- The Supreme Audit Institution is a court and its members are judges who can impose penalty corrections on audited officials;
- Professional staff in the Supreme Audit Institution tend to have legal rather than accounting or auditing backgrounds; and
- There is limited follow up of the Court’s reports by Parliament.

There can be variations from one state to another within the broad judicial model described.

Engagement partner – The partner or other person in the audit organization who is responsible for the engagement and its performance, and for the report that is issued on behalf of the audit organization, and who, where required, has the appropriate authority from a professional, legal or regulatory body.

In many jurisdictions, there is a single appointed Auditor General who acts in a role equivalent to that of “engagement partner” and who has overall responsibility for public sector audits. If, however, the Auditor General appoints an employee or other suitably qualified person to perform an audit on his/her behalf, it is the appointed auditor who effectively discharges the obligations of the engagement partner. For Supreme Audit Institutions operating in a Court of Accounts environment, the terms should be interpreted in the context of the Supreme Audit Institutions own arrangement for strategic leadership of the governing body, and definitions of responsibilities of key engagement team members. (See also IFAC Glossary of Terms).

Financial audit – An independent assessment, resulting in a reasonable assurance opinion, of whether an entity’s reported financial condition, results, and use of resources are presented fairly in accordance with the financial reporting framework. (See Regularity audit)

Firm – (See Audit organization)

Governing Board of INTOSAI – Is composed of 18 members and as a rule, it meets annually between Congresses. To ensure balanced representation of all member countries, each of INTOSAI’s seven regional working groups and the main types of public auditing systems are represented on the Board.

Government business enterprises – Include both trading enterprises, such as utilities, and financial enterprises, such as financial institutions. Government business
enterprises are, in substance no different from entities conducting similar activities in the private sector; government business enterprises generally operate to make a profit, although some may have limited community service obligations under which they are required to provide some individuals and organizations in the community with goods and services at either no charge or a significantly reduced charge.

Government business enterprises have all the following characteristics:
(a) Is an entity with the power to contract in its own name;
(b) Has been assigned the financial and operational authority to carry on a business;
(c) Sells goods and services, in the normal course of its business, to other entities at a profit or full cost recovery;
(d) Is not reliant on continuing government funding to be a going concern (other than purchases of outputs at arm’s length); and
(e) Is controlled by a public sector entity.

Government entities – a governmental office, unit, agency, bureau, department, ministry, or a consolidated group of such entities.

Independence – As defined in the Lima Declaration68 and the INTOSAI Code of Ethics69. (See also IFAC Glossary of Terms).

Instance of non-compliance with authorities – Failure to adhere to law or regulation, including budgetary authority, for an action or a transaction.

Internal control – The whole system of financial and other controls, including the organizational structure, methods, procedures and internal audit, established by management within its corporate goals, to assist in conducting the business of the audited entity in a regular economic, efficient and effective manner; ensuring adherence to management policies; safe guarding assets and resources; securing the accuracy and completeness of accounting records; and producing timely and reliable financial and management information. (See also IFAC Glossary of Terms).

Jurisdiction – The right and power to interpret and apply the law.

Legislature – An officially elected or otherwise selected body of people vested with the responsibility and power to make laws for a sovereign unit, such as a state or nation.

Legislation – A law or set of laws proposed by a government and made official by a parliament.

68 ISSAI 1 “The Lima Declaration” Section 5
69 ISSAI 30 “Code of Ethics” Chapter 3
Legislator – A member of a legislative body.

Ministry – Department of the government led by a minister.

Partner – (See Engagement Partner)

Performance audit – An audit of the economy, efficiency and effectiveness with which the audited entity uses its resources in carrying out its responsibilities, also known as Value for Money audit.

Practice Note – Included in the INTOSAI Financial Audit Guidelines. The Practice Note explains how to apply the ISA in a financial audit in the public sector. They also contain guidance relevant to audits of public sector entities in addition to what is provided for in the ISA.

Propriety – (See Compliance Audit)

Public sector auditor – A person or persons appointed under statute or agreement, a person or persons acting as the agent of a national audit agency or a Court of Accounts composed of judges.

Regularity audit – According to ISSAI 100\textsuperscript{70} regularity audit embraces:
(a) attestation of financial accountability of accountable entities, involving examination and evaluation of financial records and expression of opinions on financial statements;
(b) attestation of financial accountability of the government administration as a whole;
(c) audit of financial systems and transactions, including evaluation of compliance with applicable statutes and regulations;
(d) audit of financial systems and transactions, including evaluation of compliance with applicable statutes and regulations;
(e) audit of the probity and propriety of administrative decisions taken within the audited entity; and
(f) reporting of any other matters arising from or relating to the audit that the Supreme Audit Institution considers should be disclosed.

The terms “regularity audit” and “financial audit” are often used interchangeably. Such references to audits includes an audit of financial statements, and some or all of the elements set out in a) to above, depending on the mandate of the Supreme Audit Institution.

\textsuperscript{70}ISSAI 100 “Basic Principles in Government Auditing”
Relevant ethical requirements – As defined in the INTOSAI Code of Ethics\textsuperscript{71}. (See also IFAC Glossary of Terms).

State-owned enterprises – (See Government business enterprises)
Statutory – Decided or controlled by law.

Supreme Audit Institution – The public body of a State which, however designated, constituted or organized, exercises by virtue of law, the highest public auditing function of that State. In some Supreme Audit Institutions there are a single appointed Auditor General who acts in a role equivalent to that of “engagement partner” and who has overall responsibility for public sector audits. Other Supreme Audit Institutions may be organized as a Court of Accounts or having a collegiate or board system.

Those charged with governance – In the public sector, governance responsibilities may exist at several organizational levels as well as in several functions (i.e. vertically or horizontally). As a result, there may be instances where several distinct groups are identified as those charged with governance. Furthermore, an audit in the public sector might involve both financial statement objectives as well as compliance objectives and in some cases that may involve separate governance bodies. (See also IFAC Glossary of Terms)

GLOSSARY OF TERMS\textsuperscript{72}
(February 2009)

Access controls—Procedures designed to restrict access to on-line terminal devices, programs and data. Access controls consist of user authentication and user authorization. “User authentication” typically attempts to identify a user through unique logon identifications, passwords, access cards or biometric data. User authorization consists of access rules to determine the computer resources each user may access. Specifically, such procedures are designed to prevent or detect:

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\textsuperscript{71}ISSAI 30 "Code of Ethics"

\textsuperscript{72} In the case of public sector engagements, the terms in this glossary should be read as referring to their public sector equivalents. “This Glossary of Terms is an extract from the Handbook of International Standards on Auditing and Quality Control of the International Auditing and Assurance Standards Board, published by the International Federation of Accountants (IFAC) in April 2009 and is used with the permission of IFAC.”
(a) Unauthorized access to on-line terminal devices, programs and data;
(b) Entry of unauthorized transactions;
(c) Unauthorized changes to data files;
(d) The use of computer programs by unauthorized personnel; and
(e) The use of computer programs that have not been authorized.

* **Accounting estimate**—An approximation of a monetary amount in the absence of a precise means of measurement. This term is used for an amount measured at fair value where there is estimation uncertainty, as well as for other amounts that require estimation. Where ISA 540\(^73\) addresses only accounting estimates involving measurement at fair value, the term —fair value accounting estimates is used.

* **Accounting records**—The records of initial accounting entries and supporting records, such as checks and records of electronic fund transfers; invoices; contracts; the general and subsidiary ledgers, journal entries and other adjustments to the financial statements that are not reflected in formal journal entries; and records such as work sheets and spreadsheets supporting cost allocations, computations, reconciliations and disclosures.

* **Agreed-upon procedures engagement**—An engagement in which an auditor is engaged to carry out those procedures of an audit nature to which the auditor and the entity and any appropriate third parties have agreed and to report on factual findings. The recipients of the report form their own conclusions from the report by the auditor. The report is restricted to those parties that have agreed to the procedures to be performed since others, unaware of the reasons for the procedures may misinterpret the results.

* **Analytical procedures**\(^74\)—Evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.

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\(^73\) Where accounting terms have not been defined in the pronouncements of the International Auditing and Assurance Standards Board, reference should be made to the Glossary of Terms published by the International Accounting Standards Board.

ISA 540, —"Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures."

\(^74\) Denotes a term defined in the ISAs. Denotes a term defined in ISQC 1.
* **Annual report**—A document issued by an entity, ordinarily on an annual basis, which includes its financial statements together with the auditor’s report thereon.

* **Anomaly**—A misstatement or deviation that is demonstrably not representative of misstatements or deviations in a population.

* **Applicable financial reporting framework**—The financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation of the financial statements that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation.

The term —fair presentation frameworkǁ is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:

(a) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or

(b) Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term “compliance framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (a) or (b) above.

* **Application controls in information technology**—Manual or automated procedures that typically operate at a business process level. Application controls can be preventative or detective in nature and are designed to ensure the integrity of the accounting records. Accordingly, application controls relate to procedures used to initiate, record, process and report transactions or other financial data.

* **Applied criteria (in the context of ISA 81075)**—The criteria applied by management in the preparation of the summary financial statements.

* ** Appropriateness (of audit evidence)**—The measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor’s opinion is based.

* **Arm’s length transaction** —A transaction conducted on such terms and conditions

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75ISA 810, "Engagements to Report on Summary Financial Statements."
as between a willing buyer and a willing seller who are unrelated and are acting independently of each other and pursuing their own best interests.

* **Assertions**—Representations by management, explicit or otherwise, that are embodied in the financial statements, as used by the auditor to consider the different types of potential misstatements that may occur.

* **Assess**—Analyze identified risks of to conclude on their significance.—Assess, by convention, is used only in relation to risk. (also see Evaluate)

* **Association**—(see Auditor association with financial information)**

* **Assurance engagement**—An engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria. The outcome of the evaluation or measurement of a subject matter is the information that results from applying the criteria (also see Subject matter information). Under the International Framework for Assurance Engagements there are two types of assurance engagement a practitioner is permitted to perform: a reasonable assurance engagement and a limited assurance engagement.

* **Reasonable assurance engagement**—The objective of a reasonable assurance engagement is a reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement as the basis for a positive form of expression of the practitioner’s conclusion.

* **Limited assurance engagement**—The objective of a limited assurance engagement is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement, but where that risk is greater than for a reasonable assurance engagement, as the basis for a negative form of expression of the practitioner’s conclusion.

* **Assurance engagement risk**—The risk that the practitioner expresses an inappropriate conclusion when the subject matter information is materially misstated.

* **Audit documentation** —The record of audit procedures performed, relevant audit

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76 Engagement circumstances include the terms of the engagement, including whether it is a reasonable assurance engagement or a limited assurance engagement, the characteristics of the subject matter, the criteria to be used, the needs of the intended users, relevant characteristics of the responsible party and its environment, and other matters, for example events, transactions, conditions and practices, that may have a significant effect on the engagement.
evidence obtained, and conclusions the auditor reached (terms such as —working papers or —work papers are also sometimes used).

* Audit evidence—Information used by the auditor in arriving at the conclusions on which the auditor’s opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information. (See Sufficiency of audit evidence and Appropriateness of audit evidence.)

* Audit file—One or more folders or other storage media, in physical or electronic form, containing the records that comprise the audit documentation for a specific engagement.

* Audit firm—(see Firm)

* Audit opinion—(see Modified opinion and unmodified opinion)

* Audit risk—The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.

* Audit sampling (sampling)—The application of audit procedures to less than 100% of items within a population of audit relevance such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population.

* Audited financial statements (in the context of ISA 810)—Financial statements77audited by the auditor in accordance with ISAs, and from which the summary financial statements are derived.

* Auditor—Auditor is used to refer to the person or persons conducting the audit, usually the engagement partner or other members of the engagement team, or, as applicable, the firm. Where an ISA expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term —engagement partner rather than—auditor is used. —Engagement partner and —firm are to be read as referring to their public sector equivalents where relevant.

* Auditor association with financial information—An auditor is associated with financial information when the auditor attaches a report to that information or consents to the use of the auditor’s name in a professional connection.

* Auditor’s expert—An individual or organization possessing expertise in a field other

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77ISA 200, —Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing, paragraph 13(f), defines the term —financial statements.
than accounting or auditing, whose work in that field is used by the auditor to assist
the auditor in obtaining sufficient appropriate audit evidence. An auditor’s expert
may be either an auditor’s internal expert (who is a partner78 or staff, including
temporary staff, of the auditor’s firm or a network firm), or an auditor’s external
expert.

* Auditor’s point estimate or auditor’s range—The amount, or range of amounts,
respectively, derived from audit evidence for use in evaluating management’s point
estimate.

* Auditor’s range—(see Auditor’s point estimate)

* Business risk—A risk resulting from significant conditions, events, circumstances,
actions or inactions that could adversely affect an entity’s ability to achieve its
objectives and execute its strategies, or from the setting of inappropriate objectives
and strategies.

* Comparative financial statements—Comparative information where amounts and
other disclosures for the prior period are included for comparison with the financial
statements of the current period but, if audited, are referred to in the auditor’s
opinion.
The level of information included in those comparative financial statements is
comparable with that of the financial statements of the current period.

* Comparative information—The amounts and disclosures included in the financial
statements in respect of one or more prior periods in accordance with the applicable
financial reporting framework.

* Compilation engagement—An engagement in which accounting expertise, as
opposed to auditing expertise, is used to collect, classify and summarize financial
information.

* Complementary user entity controls—Controls that the service organization
assumes, in the design of its service, will be implemented by user entities, and
which, if necessary to achieve control objectives, are identified in the description of
its system.

* Compliance framework—(see Applicable financial reporting framework and
General purpose framework)

* Component—An entity or business activity for which group or component
management prepares financial information that should be included in the group
financial statements.

78—Partner and —firm should be read as referring to their public sector equivalents where relevant.
* **Component auditor**—An auditor who, at the request of the group engagement team, performs work on financial information related to a component for the group audit.

* **Component management**—Management responsible for the preparation of the financial information of a component.

* **Component materiality**—The materiality for a component determined by the group engagement team.

* **Computer-assisted audit techniques**—Applications of auditing procedures using the computer as an audit tool (also known as CAATs).

* **Control activities**—Those policies and procedures that help ensure that management directives are carried out. Control activities are a component of internal control.

* **Control environment**—Includes the governance and management functions and the attitudes, awareness and actions of those charged with governance and management concerning the entity’s internal control and its importance in the entity. The control environment is a component of internal control.

* **Control risk**—(see Risk of material misstatement) **Corporate governance**—(see Governance)

* **Corresponding figures**—Comparative information where amounts and other disclosures for the prior period are included as an integral part of the current period financial statements, and are intended to be read only in relation to the amounts and other disclosures relating to the current period (referred to as —current period figures). The level of detail presented in the corresponding amounts and disclosures is dictated primarily by its relevance to the current period figures.

* **Criteria**—The benchmarks used to evaluate or measure the subject matter including, where relevant, benchmarks for presentation and disclosure. Criteria can be formal or less formal. There can be different criteria for the same subject matter. Suitable criteria are required for reasonably consistent evaluation or measurement of a subject matter within the context of professional judgment.

* **Suitable criteria**—Exhibit the following characteristics:
  
  (a) Relevance: relevant criteria contribute to conclusions that assist decision-making by the intended users.

  (b) Completeness: criteria are sufficiently complete when relevant factors that could affect the conclusions in the context of the engagement circumstances
are not omitted. Complete criteria include, where relevant benchmarks for presentation and disclosure.

(c) Reliability: reliable criteria allow reasonably consistent evaluation or measurement of the subject matter including, where relevant, presentation and disclosure, when used in similar circumstances by similarly qualified practitioners.

(d) Neutrality: neutral criteria contribute to conclusions that are free from bias.

(e) Understandability: understandable criteria contribute to conclusions that are clear, comprehensive, and not subject to significantly different interpretations.

* **Date of approval of the financial statements** —The date on which all the statements that comprise the financial statements, including the related notes, have been prepared and those with the recognized authority have asserted that they have taken responsibility for those financial statements.

* **Date of report (in relation to quality control)** —The date selected by the practitioner to date the report.

* **Date of the auditor’s report** —The date the auditor dates the report on the financial statements in accordance with ISA700.79

* **Date of the financial statements** —The date of the end of the latest period covered by the financial statements.

* **Date the financial statements are issued** —The date that the auditor’s report and audited financial statements are made available to third parties.

* **Deficiency in internal control** —This exists when:
  
  (a) A control is designed, implemented or operated in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements on a timely basis; or
  
  (b) A control necessary to prevent, or detect and correct, misstatements in the financial statements on a timely basis is missing.

* **Detection risk** —The risk that the procedures performed by the auditor to reduce audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

* **Element** —(see Element of a financial statement)

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79 ISA 700, —Forming an Opinion and Reporting on Financial Statements.1
* **Element of a financial statement (in the context of ISA 805[^80])**—An element, account or item of a financial statement.

* **Emphasis of Matter paragraph**—A paragraph included in the auditor’s report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor’s judgment, is of such importance that it is fundamental to users’ understanding of the financial statements.

* **Engagement documentation**—The record of work performed, results obtained, and conclusions the practitioner reached (terms such as “working papers” or —work papers are sometimes used).

* **Engagement letter**—Written terms of an engagement in the form of a letter.

* **Engagement partner[^81]**—The partner or other person in the firm who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.

* **Engagement quality control review**—A process designed to provide an objective evaluation, on or before the date of the report, of the significant judgments the engagement team made and the conclusions it reached in formulating the report. The engagement quality control review process is for audits of financial statements of listed entities and those other engagements, if any, for which the firm has determined an engagement quality control review is required.

* **Engagement quality control reviewer**—A partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to objectively evaluate the significant judgments the engagement team made and the conclusions it reached in formulating the report.

* **Engagement team**—All partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform procedures on the engagement. This excludes external experts engaged by the firm or a network firm[^82].

**Entity’s risk assessment process**—A component of internal control that is the entity’s process for identifying business risks relevant to financial reporting

[^80]: ISA 805, —Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement.

[^81]: Engagement partner, —partner, and —firm should be read as referring to their public sector equivalents where relevant.

[^82]: ISA 620, —Using the Work of an Auditor’s Expert, paragraph 6(a), defines the term —auditor’s expert.
objectives and deciding about actions to address those risks, and the results thereof.

* **Environmental matters**—
  (a) Initiatives to prevent, abate, or remedy damage to the environment, or to deal with conservation of renewable and non-renewable resources (such initiatives may be required by environmental laws and regulations or by contract, or they may be undertaken voluntarily);
  (b) Consequences of violating environmental laws and regulations;
  (c) Consequences of environmental damage done to others or to natural resources; and
  (d) Consequences of vicarious liability imposed by law (for example, liability for damages caused by previous owners).

* **Environmental performance report**—A report, separate from the financial statements, in which an entity provides third parties with qualitative information on the entity’s commitments towards the environmental aspects of the business, its policies and targets in that field, its achievement in managing the relationship between its business processes and environmental risk, and quantitative information on its environmental performance.

* **Environmental risk**—In certain circumstances, factors relevant to the assessment of inherent risk for the development of the overall audit plan may include the risk of material misstatement of the financial statements due to environmental matters.

* **Error**—An unintentional misstatement in financial statements, including the omission of an amount or a disclosure.

* **Estimation uncertainty**—The susceptibility of an accounting estimate and related disclosures to an inherent lack of precision in its measurement.

* **Evaluate**—Identify and analyze the relevant issues, including performing further procedures as necessary, to come to a specific conclusion on a matter. —Evaluation, by convention, is used only in relation to a range of matters, including evidence, the results of procedures and the effectiveness of management’s response to a risk. (also see Assess)

* **Exception**—A response that indicates a difference between information requested to be confirmed, or contained in the entity’s records, and information provided by the confirming party.

* **Experienced auditor**—An individual (whether internal or external to the firm) who has practical audit experience, and a reasonable understanding of:
(a) Audit processes;
(b) ISAs and applicable legal and regulatory requirements;
(c) The business environment in which the entity operates; and
(d) Auditing and financial reporting issues relevant to the entity’s industry.

* Expert—(see Auditor’s expert and Management’s expert)
* Expertise—Skills, knowledge and experience in a particular field.
* External confirmation—Audit evidence obtained as a direct written response to the auditor from a third party (the confirming party), in paper form, or by electronic or other medium.
* Fair presentation framework—(see Applicable financial reporting framework and General purpose framework)
* Financial statements—A structured representation of historical financial information, including related notes, intended to communicate an entity’s economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information. The term—financial statements ordinarily refers to a complete set of financial statements as determined by the requirements of the applicable financial reporting framework, but it can also refer to a single financial statement.

* Firm—A sole practitioner, partnership or corporation or other entity of professional accountants.
* Forecast—Prospective financial information prepared on the basis of assumptions as to future events which management expects to take place and the actions management expects to take as of the date the information is prepared (best-estimate assumptions).

* Fraud—An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.
* Fraud risk factors—Events or conditions that indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud.
* Fraudulent financial reporting—Involves intentional misstatements, including omissions of amounts or disclosures in financial statements, to deceive financial statement users.
* General IT- controls—Policies and procedures that relate to many applications and
support the effective functioning of application controls by helping to ensure the continued proper operation of information systems. General IT-controls commonly include controls over data center and network operations; system software acquisition, change and maintenance; access security; and application system acquisition, development, and maintenance.

* **General purpose financial statements**—Financial statements prepared in accordance with a general purpose framework.

* **General purpose framework**—A financial reporting framework designed to meet the common financial information needs of a wide range of users. The financial reporting framework may be a fair presentation framework or a compliance framework.

The term —fair presentation framework is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:

- Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or
- Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term —compliance framework is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (a) or (b) above.83

* **Governance**—Describes the role of person(s) or organization(s) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity.

* **Group**—All the components whose financial information is included in the group financial statements. A group always has more than one component.

* **Group audit**—The audit of group financial statements.

* **Group audit opinion**—The audit opinion on the group financial statements.

* **Group engagement partner**—The partner or other person in the firm who is responsible for the group audit engagement and its performance, and for the auditor’s report on the group financial statements that is issued on behalf of the firm.

Where joint auditors conduct the group audit, the joint engagement partners and their

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83 ISA 200, paragraph 13(a).
engagement teams collectively constitute the group engagement partner and the group engagement team.

* **Group engagement team**—Partners, including the group engagement partner, and staff who establish the overall group audit strategy, communicate with component auditors, perform work on the consolidation process, and evaluate the conclusions drawn from the audit evidence as the basis for forming an opinion on the group financial statements.

* **Group financial statements**—Financial statements that include the financial information of more than one component. The term—group financial statements—also refers to combined financial statements aggregating the financial information prepared by components that have no parent but are under common control.

* **Group management**—Management responsible for the preparation of the group financial statements.

* **Group-wide controls**—Controls designed, implemented and maintained by group management over group financial reporting.

* **Historical financial information**—Information expressed in financial terms in relation to a particular entity, derived primarily from that entity’s accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.

* **Inconsistency**—other information that contradicts information contained in the audited financial statements. A material inconsistency may raise doubt about the audit conclusions drawn from audit evidence previously obtained and, possibly, about the basis for the auditor’s opinion on the financial statements.

* **Independence**—Comprises:
  
  (a) Independence of mind—the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism.

  (b) Independence in appearance—the avoidance of facts and circumstances that are so significant a reasonable and informed third party, having knowledge of all relevant information, including any safeguards applied, would reasonably conclude a firm’s, or a member of the assurance team’s, integrity, objectivity or professional skepticism had been compromised.

* **Information system relevant to financial reporting**—A component of internal control

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84 As defined in the IFAC Code of Ethics for Professional Accountants.
that includes the financial reporting system, and consists of the procedures and records established to initiate, record, process and report entity transactions (as well as events and conditions) and to maintain accountability for the related assets, liabilities and equity.

* Inherent risk—(see Risk of material misstatement)

* Initial audit engagement—An engagement in which either:
  - The financial statements for the prior period were not audited; or
  - The financial statements for the prior period were audited by a predecessor auditor.

* Inquiry—Inquiry consists of seeking information of knowledgeable persons, both financial and non-financial, within the entity or outside the entity.

* Inspection (as an audit procedure)—Examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset.

* Inspection (in relation to quality control)—In relation to completed engagements, procedures designed to provide evidence of compliance by engagement teams with the firm’s quality control policies and procedures.

* Intended users—The person, persons or class of persons for whom the practitioner prepares the assurance report. The responsible party can be one of the intended users, but not the only one.

* Interim financial information or statements—Financial information (which may be less than a complete set of financial statements as defined above) issued at interim dates (usually half-yearly or quarterly) in respect of a financial period.

* Function—An appraisal activity established or provided as a service to the entity. Its functions include, amongst other things, examining, evaluating and monitoring the adequacy and effectiveness of internal control.

* Internal auditors—Those individuals who perform the activities of the internal audit function. Internal auditors may belong to an internal audit department or equivalent function.

* Internal control—The process designed, implemented and maintained by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity’s objectives with regard to reliability of
financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. The term —controls refers to any aspects of one or more of the components of internal control.


* **Investigate**—Inquire into matters arising from other procedures to resolve them.

* **IT environment**—The policies and procedures that the entity implements and the IT infrastructure (hardware, operating systems, etc.) and application software that it uses to support business operations and achieve business strategies.

* **Limited assurance engagement**—(see *Assurance engagement*)

* **Listed entity**—An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body.

* **Management**—The person(s) with executive responsibility for the conduct of the entity’s operations. For some entities in some jurisdictions, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager.

* **Management bias**—A lack of neutrality by management in the preparation of information.

* **Management’s expert**—An individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements.

* **Management’s point estimate**—The amount selected by management for recognition or disclosure in the financial statements as an accounting estimate.

* **Misappropriation of assets**—Involves the theft of an entity’s assets and is often perpetrated by employees in relatively small and immaterial amounts. However, it can also involve management who are usually more capable of disguising or concealing misappropriations in ways that are difficult to detect.

* **Misstatement**—A difference between the amount, classification, presentation, or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the
applicable financial reporting framework. Misstatements can arise from error or fraud.
Where the auditor expresses an opinion on whether the financial statements are presented fairly, in all material respects, or give a true and fair view, misstatements also include those adjustments of amounts, classifications, presentation, or disclosures that, in the auditor’s judgment, are necessary for the financial statements to be presented fairly, in all material respects, or to give a true and fair view.

* **Misstatement of fact**—Other information that is unrelated to matters appearing in the audited financial statements that is incorrectly stated or presented. A material misstatement of fact may undermine the credibility of the document containing audited financial statements.

* **Modified opinion**—A qualified opinion, an adverse opinion or a disclaimer of opinion.

* **Monitoring (in relation to quality control)**—A process comprising an ongoing consideration and evaluation of the firm’s system of quality control, including a periodic inspection of a selection of completed engagements, designed to provide the firm with reasonable assurance that its system of quality control is operating effectively.

* **Monitoring of controls**—A process to assess the effectiveness of internal control performance over time. It includes assessing the design and operation of controls on a timely basis and taking necessary corrective actions modified for changes in conditions. Monitoring of controls is a component of internal control.

* **Negative confirmation request**—A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.

* **Network**—A larger structure:
  (a) That is aimed at cooperation, and
  (b) That is clearly aimed at profit or cost-sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.

* **Network firm**—A firm or entity that belongs to a network.
* **Non-compliance (in the context of ISA 250)**—Acts of omission or commission by the entity, either intentional or unintentional, which are contrary to the prevailing laws or regulations. Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or employees. Non-compliance does not include personal misconduct (unrelated to the business activities of the entity) by those charged with governance, management or employees of the entity.

* **Non-response**—A failure of the confirming party to respond, or fully respond, to a positive confirmation request, or a confirmation request returned undelivered.

* **Non-sampling risk**—The risk that the auditor reaches an erroneous conclusion for any reason not related to sampling risk.

* **Observation**—Consists of looking at a process or procedure being performed by others, for example, the auditor’s observation of inventory counting by the entity’s personnel, or of the performance of control activities.

* **Opening balances**—Those account balances that exist at the beginning of the period. Opening balances are based upon the closing balances of the prior period and reflect the effects of transactions and events of prior periods and accounting policies applied in the prior period. Opening balances also include matters requiring disclosure that existed at the beginning of the period, such as contingencies and commitments.

* **Other information**—Financial and non-financial information (other than the financial statements and the auditor’s report thereon) which is included, either by law, regulation, or custom, in a document containing audited financial statements and the auditor’s report thereon.

* **Other Matter paragraph**—A paragraph included in the auditor’s report that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor’s judgment, is relevant to users’ understanding of the audit, the auditor’s responsibilities or the auditor’s report.

* **Outcome of an accounting estimate**—The actual monetary amount which results from the resolution of the underlying transaction(s), event(s) or condition(s) addressed by the accounting estimate.

* **Overall audit strategy**—Sets the scope, timing and direction of the audit, and guides the development of the more detailed audit plan.

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85 ISA 250, - Consideration of Laws and Regulations in an Audit of Financial Statements.
* Partner—Any individual with authority to bind the firm with respect to the performance of a professional services engagement.

* Performance materiality—The amount or amounts set by the auditor at less than materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. If applicable, performance materiality also refers to the amount or amounts set by the auditor at less than the materiality level or levels for particular classes of transactions, account balances or disclosures.

* Personnel—Partners and staff.

* Pervasive—A term used, in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence. Pervasive effects on the financial statements are those that, in the auditor’s judgment:

  (a) Are not confined to specific elements, accounts or items of the financial statements;

  (b) If so confined, represent or could represent a substantial proportion of the financial statements; or

  (c) In relation to disclosures, are fundamental to users’ understanding of the financial statements.

* Population—The entire set of data from which a sample is selected and about which the auditor wishes to draw conclusions.

* Positive confirmation request—A request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the requested information.

* Practitioner—A professional accountant in public practice.

* Preconditions for an audit—The use by management of an acceptable financial reporting framework in the preparation of the financial statements and the agreement of management and, where appropriate, those charged with governance to the premise on which an audit is conducted.

* Predecessor auditor—The auditor from a different audit firm, who audited the

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86 ISA 200, paragraph 13.
financial statements of an entity in the prior period and who has been replaced by the current auditor.

* Premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit is conducted—That management and, where appropriate, those charged with governance have acknowledged and understand that they have the following responsibilities that are fundamental to the conduct of an audit in accordance with ISAs. That is, responsibility:

- For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation;
- For such internal control as management and, where appropriate, those charged with governance determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
- To provide the auditor with:
  
  (i) Access to all information of which management and, where appropriate, those charged with governance are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
  
  (ii) Additional information that the auditor may request from management and, where appropriate, those charged with governance for the purpose of the audit; and
  
  (iii) Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

In the case of a fair presentation framework, (a) above may be restated as —for the preparation and fair presentation of the financial statements in accordance with the financial reporting framework, or —for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework.

The —premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit is conducted may also be referred to as the premise.

* Professional accountant\(^\text{87}\)—An individual who is a member of an IFAC member body.

\(^{87}\) As defined in the IFAC Code of Ethics for Professional Accountants.
* **Professional accountant in public practice**—A professional accountant, irrespective of functional classification (for example, audit, tax or consulting) in a firm that provides professional services. This term is also used to refer to a firm of professional accountants in public practice.

* **Professional judgment**—The application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.

* **Professional skepticism**—An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of evidence.

* **Professional standards**—International Standards on Auditing (ISAs) and relevant ethical requirements

* **Professional standards (in the context of ISQC 1)**—IAASB Engagement Standards, as defined in the IAASB’s Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services, and relevant ethical requirements.

* **Projection**—Prospective financial information prepared on the basis of:

  (a) Hypothetical assumptions about future events and management actions which are not necessarily expected to take place, such as when some entities are in a start-up phase or are considering a major change in the nature of operations; or

  (b) A mixture of best-estimate and hypothetical assumptions.

* **Prospective financial information**—financial information based on assumptions about events that may occur in the future and possible actions by an entity. Prospective financial information can be in the form of a forecast, a projection or a combination of both. (see **Forecast** and **Projection**)

* **Public sector**—National governments, regional (for example, state, provincial, territorial) governments, local (for example, city, town) governments and related governmental entities (for example, agencies, boards, commissions and enterprises).

* **Reasonable assurance (in the context of assurance engagements, including audit engagements, and quality control)**—A high, but not absolute, level of assurance.

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88 As defined in the IFAC Code of Ethics for Professional Accountants.

89 ISQC 1, —Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements.
* **Reasonable assurance engagement**—(see Assurance engagement)

* **Recalculation**—consists of checking the mathematical accuracy of documents or records.

* **Related party**—A party that is either:
  (a) A related party as defined in the applicable financial reporting framework; or
  (b) Where the applicable financial reporting framework establishes minimal or no related party requirements:
    (i) A person or other entity that has control or significant influence, directly or indirectly through one or more intermediaries, over the reporting entity;
    (ii) Another entity over which the reporting entity has control or significant influence, directly or indirectly through one or more intermediaries; or
    (iii) Another entity that is under common control with the reporting entity through having:
      a) Common controlling ownership;
      b) Owners who are close family members; or
      c) Common key management.

However, entities that are under common control by a state (that is, a national, regional or local government) are not considered related unless they engage in significant transactions or share resources to a significant extent with one another.

* **Related services**—comprise agreed-upon procedures and compilations.

* **Relevant ethical requirements**—Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Parts A and B of the International Federation of Accountants’ *Code of Ethics for Professional Accountants* (IFAC Code) together with national requirements that are more restrictive.

* **Re-performance**—The auditor’s independent execution of procedures or controls that were originally performed as part of the entity’s internal controls.

* **Report on the description and design of controls at a service organization (referred to in ISA 40290 as a type 1 report)**—A report that comprises:
  (a) A description, prepared by management of the service organization, of the service organization’s system, control objectives and related controls that have been designed and implemented as at a specified date; and

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90ISA 402, —Audit Considerations Relating to an Entity Using a Service Organization.
(b) A report by the service auditor with the objective of conveying reasonable assurance that includes the service auditor’s opinion on the description of the service organization’s system, control objectives and related controls and the suitability of the design of the controls to achieve the specified control objectives.

* **Report on the description, design, and operating effectiveness of controls at a service organization (referred to in ISA 402 as a type 2 report)—**A report that comprises:

  (a) A description, prepared by management of the service organization, of the service organization’s system, control objectives and related controls, their design and implementation as at a specified date or throughout a specified period and, in some cases, their operating effectiveness throughout a specified period; and

  (b) A report by the service auditor with the objective of conveying reasonable assurance that includes:

    (i) The service auditor’s opinion on the description of the service organization’s system, control objectives and related controls, the suitability of the design of the controls to achieve the specified control objectives, and the operating effectiveness of the controls; and

    (ii) A description of the service auditor’s tests of the controls and the results thereof.

* **Responsible party—**The person (or persons) who:

  (a) In a direct reporting engagement, is responsible for the subject matter; or

  (b) In an assertion-based engagement, is responsible for the subject matter information (the assertion), and may be responsible for the subject matter. The responsible party may or may not be the party who engages the practitioner (the engaging party).

* **Review (in relation to quality control)—**Appraising the quality of the work performed and conclusions reached by others.

* **Review engagement—**The objective of a review engagement is to enable an auditor to state whether, on the basis of procedures which do not provide all the evidence that would be required in an audit, anything has come to the auditor’s attention that causes the auditor to believe that the financial statements are not prepared, in all material respects, in accordance with an applicable financial reporting framework.
* **Review procedures**—The procedures deemed necessary to meet the objective of are view engagement, primarily inquiries of entity personnel and analytical procedures applied to financial data.

* **Risk assessment procedures**—The audit procedures performed to obtain an understanding of the entity and its environment, including the entity’s internal control, to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels.

* **Risk of material misstatement**—The risk that the financial statements are materially misstated prior to audit. This consists of two components, described as follows at the assertion level:

(a) **Inherent risk**—The susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.

(b) **Control risk**—The risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity’s internal control.

* **Sampling**—(see *Audit sampling*)

* **Sampling risk**—The risk that the auditor’s conclusion based on a sample may be different from the conclusion if the entire population were subjected to the same audit procedure. Sampling risk can lead to two types of erroneous conclusions:

(a) In the case of a test of controls, that controls are more effective than they actually are, or in the case of a test of details, that a material misstatement does not exist when in fact it does. The auditor is primarily concerned with this type of erroneous conclusion because it affects audit effectiveness and is more likely to lead to an inappropriate audit opinion.

(b) In the case of a test of controls, that controls are less effective than they actually are, or in the case of a test of details, that a material misstatement exists when in fact it does not. This type of erroneous conclusion affects audit efficiency as it would usually lead to additional work to establish that initial conclusions were incorrect.

* **Sampling unit**—The individual items constituting a population.
* **Scope of a review**—The review procedures deemed necessary in the circumstances to achieve the objective of the review.

* **Service auditor**—An auditor who, at the request of the service organization, provides an assurance report on the controls of a service organization.

* **Service organization**—A third-party organization (or segment of a third-party organization) that provides services to user entities that are part of those entities’ information systems relevant to financial reporting.

* **Service organization’s system**—The policies and procedures designed, implemented and maintained by the service organization to provide user entities with the services covered by the service auditor’s report.

* **Significance**—The relative importance of a matter, taken in context. The significance of matter is judged by the practitioner in the context in which it is being considered. This might include, for example, the reasonable prospect of its changing or influencing the decisions of intended users of the practitioner’s report; or, as another example, where the context is a judgment about whether to report a matter to those charged with governance, whether the matter would be regarded as important by them in relation to their duties. Significance can be considered in the context of quantitative and qualitative factors, such as relative magnitude, the nature and effect on the subject matter and the expressed interests of intended users or recipients.

* **Significant component**—A component identified by the group engagement team (i) that is of individual financial significance to the group, or (ii) that, due to its specific nature or circumstances, is likely to include significant risks of material misstatement of the group financial statements.

* **Significant deficiency in internal control**—A deficiency or combination of deficiencies in internal control that, in the auditor’s professional judgment, is of sufficient importance to merit the attention of those charged with governance.

* **Significant risk**—An identified and assessed risk of material misstatement that, in the auditor’s judgment, requires special audit consideration.

* **Smaller entity**—An entity which typically possesses qualitative characteristics such as:

  (a) Concentration of ownership and management in a small number of individuals (often a single individual – either a natural person or another enterprise that owns the entity provided the owner exhibits the relevant qualitative characteristics); and
(b) One or more of the following:
   (i) Straightforward or uncomplicated transactions;
   (ii) Simple record-keeping;
   (iii) Few lines of business and few products within business lines;
   (iv) Few internal controls;
   (v) Few levels of management with responsibility for a broad range of controls; or
   (vi) Few personnel, many having a wide range of duties.

These qualitative characteristics are not exhaustive, they are not exclusive to smaller entities, and smaller entities do not necessarily display all of these characteristics.

* **Special purpose financial statements**—Financial statements prepared in accordance with a special purpose framework.

* **Special purpose framework**—A financial reporting framework designed to meet the financial information needs of specific users. The financial reporting framework may be a fair presentation framework or a compliance framework.91

* **Staff**—Professionals, other than partners, including any experts the firm employs.

* **Statistical sampling**—An approach to sampling that has the following characteristics:
   (a) Random selection of the sample items; and
   (b) The use of probability theory to evaluate sample results, including measurement of sampling risk.

A sampling approach that does not have characteristics (a) and (b) is considered non-statistical sampling.

* **Stratification**—The process of dividing a population into sub-populations, each of which is a group of sampling units which have similar characteristics (often monetary value).

* **Subject matter information**—The outcome of the evaluation or measurement of a subject matter. It is the subject matter information about which the practitioner gathers sufficient appropriate evidence to provide a reasonable basis for expressing a conclusion in an assurance report.

* **Subsequent events**—Events occurring between the date of the financial statements and the date of the auditor’s report, and facts that become known to the auditor after the date of the auditor’s report.

* **Subservice organization**—A service organization used by another service organization to perform some of the services provided to user entities that are part of

91 ISA 200, paragraph 13(a).
those user entities’ information systems relevant to financial reporting.

* **Substantive procedure**—An audit procedure designed to detect material misstatements at the assertion level. Substantive procedures comprise:
  Tests of details (of classes of transactions, account
  (a) balances, and disclosures); and
  (b) Substantive analytical procedures.

* **Sufficiency (of audit evidence)**—The measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor’s assessment of the risks of material misstatement and also by the quality of such audit evidence.

* **Suitable criteria**—(see Criteria)

* **Suitably qualified external person**—An individual outside the firm with the competence and capabilities to act as an engagement partner, for example a partner of another firm, or an employee (with appropriate experience) of either a professional accountancy body whose members may perform audits and reviews of historical financial information, or other assurance or related services engagements, or of an organization that provides relevant quality control services.

* **Summary financial statements (in the context of ISA 810)**—Historical financial information that is derived from financial statements but that contains less detail than the financial statements, while still providing a structured representation consistent with that provided by the financial statements of the entity’s economic resources or obligations at a point in time or the changes therein for a period of time. Different jurisdictions may use different terminology to describe such historical financial information.

* **Supplementary information**—Information that is presented together with the financial statements that is not required by the applicable financial reporting framework used to prepare the financial statements, normally presented in either supplementary schedules or as additional notes.

* **Test**—The application of procedures to some or all items in a population.

* **Tests of controls**—An audit procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level.

* **Those charged with governance**—The person(s) or organization(s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the

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92 ISA 200, paragraph 13(f).
entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager. 

* **Tolerable misstatement**—A monetary amount set by the auditor in respect of which the auditor seeks to obtain an appropriate level of assurance that the monetary amount set by the auditor is not exceeded by the actual misstatement in the population.

* **Total rate of deviation**—A rate of deviation from prescribed internal control procedures set by the auditor in respect of which the auditor seeks to obtain an appropriate level of assurance that the rate of deviation set by the auditor is not exceeded by the actual rate of deviation in the population.

* **Uncertainty**—A matter whose outcome depends on future actions or events not under the direct control of the entity but that may affect the financial statements.

* **Uncorrected misstatements**—Misstatements that the auditor has accumulated during the audit and that have not been corrected.

* **Unmodified opinion**—The opinion expressed by the auditor when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

* **User auditor**—An auditor who audits and reports on the financial statements of a user entity.

* **User entity**—An entity that uses a service organization and whose financial statements are being audited.

* **Walk-through test**—Involves tracing a few transactions through the financial reporting system.

* **Written representation** — A written statement by management provided to the auditor to confirm certain matters or to support other audit evidence. Written representations in this context do not include financial statements, the assertions therein, or supporting books and records.

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93 For discussion of the diversity of governance structures, see paragraphs A1-A8 of ISA 260, —Communication with Those Charged with Governance.

94 ISA 700, paragraphs 35-36, deal with the phrases used to express this opinion in the case of a fair presentation framework and a compliance framework respectively.
ISSAI 1200

Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing

The International Standards of Supreme Audit Institutions, ISSAI, are issued by the International Organization of Supreme Audit Institutions, INTOSAI. For more information visit www.issai.org.
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Overall Objectives of the Independent Auditor

Conduct of an Audit in Accordance with International Standards on Auditing

Introduction to the ISA

ISA 200 deals with the independent auditor’s overall responsibilities when conducting an audit of financial statements in accordance with ISAs. Specifically, it sets out the overall objectives of the independent auditor, and explains the nature and scope of an audit designed to enable the independent auditor to meet those objectives. It also explains the scope, authority and structure of the ISAs, and includes requirements establishing the general responsibilities of the independent auditor applicable in all audits, including the obligation to comply with the ISAs. The independent auditor is referred to as “the auditor” hereafter.

Scope of the ISA

P4. The ISAs are written in the context of an audit of financial statements. In the INTOSAI context an audit of financial statements may be a part of a broader regularity (financial) audit. In accordance with ISSAI 100, paragraph 39, a regularity (financial) audit embraces:

(a) Attestation of financial accountability of accountable entities, involving examination and evaluation of financial records and expression of opinions on financial statements;
(b) Attestation of financial accountability of the government administration as a whole;

All Practice Notes are considered together with ISSAI 100 “General Introduction to the INTOSAI Financial Audit Guidelines.”

ISA 200 paragraph A1: The auditor’s opinion on the financial statements deals with whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework. Such an opinion is common to all audits of financial statements. The auditor’s opinion therefore does not assure, for example, the future viability of the entity nor the efficiency or effectiveness with which management has conducted the affairs of the entity. In some jurisdictions, however, applicable law or regulation may require auditors to provide opinions on other specific matters, such as the effectiveness of internal control, or the consistency of a separate management report with the financial statements. While the ISAs include requirements and guidance in relation to such matters to the extent that they are relevant to forming an opinion on the financial statements, the auditor would be required to undertake further work if the auditor had additional responsibilities to provide such opinions.

ISSAI 100, “INTOSAI Auditing Standards – Basic Principles.”
(c) Audit of financial systems and transactions including an evaluation of compliance with applicable statutes and regulations;
(d) Audit of internal control and internal audit functions;
(e) Audit of the probity and propriety of administrative decisions taken within the audited entity; and
(f) Reporting of any other matters arising from or relating to the audit that the Supreme Audit Institution considers should be disclosed.

P5. The terms ‘regularity audit’ and ‘financial audit’ are often used interchangeably. Such audits consist of an audit of financial statements, plus some or all of the elements set out in a) to f) above, depending on the mandate of the Supreme Audit Institution. The Practice Notes in the INTOSAI Financial Audit Guidelines (ISSAI 1000-2999) provide additional guidance to public sector auditors when applying the ISAs in an audit of financial statements. When performing the broader ‘regularity’ or ‘financial’ audit in the public sector, more comprehensive guidance may be found in the ISSAI framework which, for example, includes the INTOSAI Compliance Audit Guidelines (ISSAI 4000 and 4200).

P6. Regularity (financial) audits are performed in a variety of environments. In financial reporting environments moving towards internationally recognized practices, the full application of ISSAIs 1000-2999 by public sector auditors will assist in providing additional structure to transforming the environment in which the audit takes place, towards internationally recognized practice.

P7. In the public sector, reference to relevant auditing standards can be made in one of the following ways depending on the standards applied:
(a) In accordance with the ISAs; which means full compliance with all relevant ISAs and if relevant, with the additional guidance set out in the INTOSAI Practice Notes to the ISAs;
(b) In accordance with the INTOSAI Fundamental Auditing Principles, but not full compliance with the ISAs which are presently included as part of the INTOSAI Financial Audit Guidelines (ISSAIs 1000-2999); or
(c) In accordance with other national and relevant Auditing Standards.

P8. In the public sector context, the Practice Notes use the term “public sector auditors” as equivalent to “the auditor” as used in the ISAs.

P9. Some ISAs contain considerations specific to audits of smaller entities. In audits of public sector entities and entities that receive government awards, these
considerations are usually not applicable, even if the public sector entity has few employees, simple operations, or a relatively small budget. In those situations, the public sector entity may still have complicated transactions, such as transfers from other governments, as well as a need to comply with laws, regulations, policies and systems determined by a higher level of government and a need for accountability for use of taxpayer monies. Therefore public sector auditors carefully consider the relevance of such considerations. The Practice Notes may include additional guidance in this area when considered important to add guidance relevant for audits of smaller public sector entities.

**An Audit of Financial Statements**

P10. When considering paragraph 6 of the ISA, public sector auditors consider further guidance included in the Practice Note to ISA 320100.

P11. Paragraph A7 of the ISA is one of many paragraphs that deal with fair presentation frameworks. The International Public Sector Accounting Standards (IPSAS), issued by the International Public Sector Accounting Standards Board is an example of a fair presentation framework designed for use in the public sector.

P12. Paragraph A8 of the ISA provides examples of financial statements and the content of a complete set of financial statements. A complete set of financial statements for a public sector entity prepared on an accrual basis of accounting may normally comprise:

- A statement of financial position;
- A statement of financial performance;
- A statement of changes in net assets/equity;
- A cash flow statement;
- A comparison of budget and actual amounts either as a separate additional financial statement or as a reconciliation; and
- Notes, comprising a summary of significant accounting policies and other explanatory information.

P13. In certain environments a complete set of financial statements may also include other reports such as reports on performance and appropriation reports.

P14. When considering paragraph A10 of the ISA, public sector auditors consider further guidance included in Practice Notes to ISA 210101 and to ISA 580102.

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100ISA 320, “Materiality in Planning and Performing an Audit.”
Overall Objectives of the Auditor

P15. Withdrawal from the engagement as described in paragraphs 12 and 24 of the ISA is normally not an option in a public sector audit. Where circumstances arise that normally will result in withdrawal from the engagement, the responsibilities of public sector auditors may include expanded or enhanced reporting, for example to the legislature.

Definitions

P16. When considering the definitions in paragraph 13 of the ISA public sector auditors take note of the following:

(a) Applicable Financial Reporting Framework – as is the case in the private sector, frameworks in the public sector may be either fair presentation or compliance frameworks; and

(b) Auditor – The terms “Engagement partner” and “Firm.” The term “Engagement partner” may, for example, refer to an Auditor General who has overall responsibility for public sector audits or another suitably qualified person delegated to or appointed on his/her behalf with responsibility for the specific engagement. The term “Firm” may normally be read as Supreme Audit Institution or equivalent at regional or local level.

Ethical Requirements Relating to an Audit of Financial Statements

P17. The INTOSAI Code of Ethics\textsuperscript{103} is a relevant ethical code in so far as paragraph 14 of the ISA is concerned.

P18. Paragraph 15 of the ISA requires the auditor to plan and perform an audit with professional skepticism recognizing that circumstances may exist that cause the financial statements to be materially misstated. The INTOSAI Fundamental Principles ISSAI 200\textsuperscript{104} address the concept of due care and state: “...Auditors need to be alert for situations, control weaknesses, inadequacies in record keeping, errors and unusual transactions or results which could be indicative of fraud, improper or unlawful expenditure, unauthorized operations, waste, inefficiency or lack of probity.” The concept of professional skepticism enhances and broadens the concept of due care and is fundamental for planning and performance of the audit.

\textsuperscript{101}ISA 210, “Agreeing the Terms of Audit Engagements.”

\textsuperscript{102}ISA 580, “Written Representations.”

\textsuperscript{103}ISSAI 30, “INTOSAI Code of Ethics.”

\textsuperscript{104}ISSAI 200, “INTOSAI Auditing Standards - General Standards,” paragraph 2.
Conduct of an Audit in Accordance with ISAs

P19. When considering paragraphs 18 to 20 of the ISA on compliance with ISAs relevant to the audit, public sector auditors also consider that in applying the ISSAIs for regularity (financial) audit in the public sector, the ISAs and the Practice Notes together form guidance for public sector auditors. If reference is made in the auditor’s report to the audit having been conducted in accordance with the ISAs, public sector auditors have to comply with all the ISAs relevant to the audit as set out in paragraphs 18-20 of the ISA.

Sufficient and Appropriate Audit Evidence and Audit Risk

P20. When considering sources of information as discussed in paragraph A28 of the ISA public sector auditors may also consider using information from previous performance audits and other audit activities relevant to the entity. They would do this only if the information is still relevant and reliable.
International Standard on Auditing

Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing
Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the independent auditor’s overall responsibilities when conducting an audit of financial statements in accordance with ISAs. Specifically, it sets out the overall objectives of the independent auditor, and explains the nature and scope of an audit designed to enable the independent auditor to meet those objectives. It also explains the scope, authority and structure of the ISAs, and includes requirements establishing the general responsibilities of the independent auditor applicable in all audits, including the obligation to comply with the ISAs. The independent auditor is referred to as “the auditor” hereafter.

2. ISAs are written in the context of an audit of financial statements by an auditor. They are to be adapted as necessary in the circumstances when applied to audits of other historical financial information. ISAs do not address the responsibilities of the auditor that may exist in legislation, regulation or otherwise in connection with, for example, the offering of securities to the public. Such responsibilities may differ from those established in the ISAs. Accordingly, while the auditor may find aspects of the ISAs helpful in such circumstances, it is the responsibility of the auditor to ensure compliance with all relevant legal, regulatory or professional obligations.

An Audit of Financial Statements

3. The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. In the case of most general purpose frameworks, that opinion is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view in accordance with the framework. An audit conducted in accordance with ISAs and relevant ethical requirements enables the auditor to form that opinion. (Ref: Para. A1)

4. The financial statements subject to audit are those of the entity, prepared by management of the entity with oversight from those charged with governance. ISAs do not impose responsibilities on management or those charged with governance and do not override laws and regulations that govern their responsibilities. However, an audit in accordance with ISAs is conducted on the premise that
management and, where appropriate, those charged with governance have acknowledged certain responsibilities that are fundamental to the conduct of the audit. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities. (Ref: Para. A2-A11)

5. As the basis for the auditor’s opinion, ISAs require the auditor to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. Reasonable assurance is a high level of assurance. It is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk (that is, the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level. However, reasonable assurance is not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor’s opinion being persuasive rather than conclusive. (Ref: Para. A28-A52)

6. The concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements. In general, misstatements, including omissions, are considered to be material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. Judgments about materiality are made in the light of surrounding circumstances, and are affected by the auditor’s perception of the financial information needs of users of the financial statements, and by the size or nature of a misstatement, or a combination of both. The auditor’s opinion deals with the financial statements as a whole and therefore the auditor is not responsible for the detection of misstatements that are not material to the financial statements as a whole.

7. The ISAs contain objectives, requirements and application and other explanatory material that are designed to support the auditor in obtaining reasonable assurance. The ISAs require that the auditor exercise professional judgment and maintain professional skepticism throughout the planning and performance of the audit and, among other things:

• Identify and assess risks of material misstatement, whether due to fraud or error, based on an understanding of the entity and its environment, including the entity’s internal control.
• Obtain sufficient appropriate audit evidence about whether material misstatements exist, through designing and implementing appropriate responses to the assessed risks.
• Form an opinion on the financial statements based on conclusions drawn from the audit evidence obtained.

8. The form of opinion expressed by the auditor will depend upon the applicable financial reporting framework and any applicable law or regulation. (Ref: Para. A12-A13)

9. The auditor may also have certain other communication and reporting responsibilities to users, management, those charged with governance, or parties outside the entity, in relation to matters arising from the audit. These may be established by the ISAs or by applicable law or regulation.106

Overall Objectives of the Auditor

11. In conducting an audit of financial statements, the overall objectives of the auditor are:
   (a) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and
   (b) To report on the financial statements, and communicate as required by the ISAs, in accordance with the auditor’s findings.

12. In all cases when reasonable assurance cannot be obtained and a qualified opinion in the auditor’s report is insufficient in the circumstances for purposes of reporting to the intended users of the financial statements, the ISAs require that the auditor disclaim an opinion or withdraw (or resign)107 from the engagement, where withdrawal is possible under applicable law or regulation.

Definitions

13. For purposes of the ISAs, the following terms have the meanings attributed below:
   (a) Applicable financial reporting framework—The financial reporting framework adopted by management and, where appropriate, those charged with

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106 See, for example, ISA 260, “Communication with Those Charged with Governance ;” and paragraph 43 of ISA 240, “The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements.”
107 In the ISAs, only the term “withdrawal” is used.
governance in the preparation of the financial statements that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation.

The term “fair presentation framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:

(i) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or

(ii) Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term “compliance framework” is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (i) or (ii) above.

(b) Audit evidence – Information used by the auditor in arriving at the conclusions on which the auditor’s opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information. For purposes of the ISAs:

(i) Sufficiency of audit evidence is the measure of the quantity of audit evidence. The quantity of the audit evidence needed is affected by the auditor’s assessment of the risks of material misstatement and also by the quality of such audit evidence.

(ii) Appropriateness of audit evidence is the measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor’s opinion is based.

(c) Audit risk – The risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.

(d) Auditor – “Auditor” is used to refer to the person or persons conducting the audit, usually the engagement partner or other members of the engagement team, or, as applicable, the firm. Where an ISA expressly intends that a requirement or responsibility be fulfilled by the engagement partner, the term “engagement partner” rather than “auditor” is used. “Engagement partner” and “firm” are to be read as referring to their public sector equivalents where relevant.

(e) Detection risk – The risk that the procedures performed by the auditor to reduce
audit risk to an acceptably low level will not detect a misstatement that exists and that could be material, either individually or when aggregated with other misstatements.

(f) Financial statements – A structured representation of historical financial information, including related notes, intended to communicate an entity’s economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information. The term “financial statements” ordinarily refers to a complete set of financial statements as determined by the requirements of the applicable financial reporting framework, but can also refer to a single financial statement.

(g) Historical financial information – Information expressed in financial terms in relation to a particular entity, derived primarily from that entity’s accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.

(h) Management–The person(s) with executive responsibility for the conduct of the entity’s operations. For some entities in some jurisdictions, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager.

(i) Misstatement – A difference between the amount, classification, presentation, or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework. Misstatements can arise from error or fraud.

Where the auditor expresses an opinion on whether the financial statements are presented fairly, in all material respects, or give a true and fair view, misstatements also include those adjustments of amounts, classifications, presentation, or disclosures that, in the auditor’s judgment, are necessary for the financial statements to be presented fairly, in all material respects, or to give a true and fair view.

(j) Premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit is conducted – That management and, where appropriate, those charged with governance have acknowledged and understand that they have the following responsibilities that are fundamental to the conduct of an audit in accordance with ISAs. That is, responsibility:
(i) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation;

(ii) For such internal control as management and, where appropriate, those charged with governance determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and

(iii) To provide the auditor with:

   a. Access to all information of which management and, where appropriate, those charged with governance are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;

   b. Additional information that the auditor may request from management and, where appropriate, those charged with governance for the purpose of the audit; and

   c. Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

In the case of a fair presentation framework, (i) above may be restated as “for the preparation and fair presentation of the financial statements in accordance with the financial reporting framework,” or “for the preparation of financial statements that give a true and fair view in accordance with the financial reporting framework.”

The “premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit is conducted” may also be referred to as the “premise.”

(k) Professional judgment – The application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.

(l) Professional skepticism – An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.

(m) Reasonable assurance – In the context of an audit of financial statements, a high, but not absolute, level of assurance.

(n) Risk of material misstatement – The risk that the financial statements are
materially misstated prior to audit. This consists of two components, described as follows at the assertion level:

(i) Inherent risk – The susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.

(ii) Control risk–The risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity’s internal control.

(o) Those charged with governance – The person(s) or organization(s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

Requirements

Sufficient Appropriate Audit Evidence and Audit Risk

14. To obtain reasonable assurance, the auditor shall obtain sufficient appropriate audit evidence to reduce audit risk to an acceptably low level and thereby enable the auditor to draw reasonable conclusions on which to base the auditor’s opinion. (Ref: Para. A28-A52)

Conduct of an Audit in Accordance with ISAs

Complying with ISAs Relevant to the Audit

15. The auditor shall comply with all ISAs relevant to the audit. An ISA is relevant to the audit when the ISA is in effect and the circumstances addressed by the ISA exist. (Ref: Para. A53 -A57)

16. The auditor shall have an understanding of the entire text of an ISA, including its application and other explanatory material, to understand its objectives and to apply its requirements properly. (Ref: Para. A58-A66)

17. The auditor shall not represent compliance with ISAs in the auditor’s report unless the auditor has complied with the requirements of this ISA and all other ISAs relevant to the audit.
Objectives Stated in Individual ISAs

21. To achieve the overall objectives of the auditor, the auditor shall use the objectives stated in relevant ISAs in planning and performing the audit, having regard to the interrelationships among the ISAs, to: (Ref: Para. A67-A69)

(a) Determine whether any audit procedures in addition to those required by the ISAs are necessary in pursuance of the objectives stated in the ISAs; and (Ref: Para. A70)
(b) Evaluate whether sufficient appropriate audit evidence has been obtained. (Ref: Para. A71)

Complying with Relevant Requirements

22. Subject to paragraph 23, the auditor shall comply with each requirement of an ISA unless, in the circumstances of the audit:

(a) The entire ISA is not relevant; or

(b) The requirement is not relevant because it is conditional and the condition does not exist. (Ref: Para. A72-A73)

23. In exceptional circumstances, the auditor may judge it necessary to depart from a relevant requirement in an ISA. In such circumstances, the auditor shall perform alternative audit procedures to achieve the aim of that requirement. The need for the auditor to depart from a relevant requirement is expected to arise only where the requirement is for a specific procedure to be performed and, in the specific circumstances of the audit, that procedure would be ineffective in achieving the aim of the requirement. (Ref: Para. A74)

Failure to Achieve an Objective

24. If an objective in a relevant ISA cannot be achieved, the auditor shall evaluate whether this prevents the auditor from achieving the overall objectives of the auditor and thereby requires the auditor, in accordance with the ISAs, to modify the auditor’s opinion or withdraw from the engagement (where withdrawal is possible under applicable law or regulation). Failure to achieve an objective represents significant matter requiring documentation in accordance with ISA 230.108 (Ref: Para. A75-A76)

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108ISA 230, “Audit Documentation,” paragraph 8(c).
Application and Other Explanatory Material

An Audit of Financial Statements

Scope of the Audit (Ref: Para. 3)

A1. The auditor’s opinion on the financial statements deals with whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework. Such an opinion is common to all audits of financial statements. The auditor’s opinion therefore does not assure, for example, the future viability of the entity nor the efficiency or effectiveness with which management has conducted the affairs of the entity. In some jurisdictions, however, applicable law or regulation may require auditors to provide opinions on other specific matters, such as the effectiveness of internal control, or the of a separate management report with the financial statements. While the ISAs include requirements and guidance in relation to such matters to the extent that they are relevant to forming an opinion on the financial statements, the auditor would be required to undertake further work if the auditor had additional responsibilities to provide such opinions.

Preparation of the Financial Statements (Ref: Para. 4)

A2. Law or regulation may establish the responsibilities of management and, where appropriate, those charged with governance in relation to financial reporting. However, the extent of these responsibilities, or the way in which they are described, may differ across jurisdictions. Despite these differences, an audit in accordance with ISAs is conducted on the premise that management and, where appropriate, those charged with governance have acknowledged and understand that they have responsibility:

  a) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation;
  b) For such internal control as management and, where appropriate, those charged with governance determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
  c) To provide the auditor with:

   (i) Access to all information of which management and, where appropriate, those charged with governance are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
(ii) Additional information that the auditor may request from management and, where appropriate, those charged with governance for the purpose of the audit; and

(iii) Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

A3. The preparation of the financial statements by management and, where appropriate, those charged with governance requires:

- The identification of the applicable financial reporting framework, in the context of any relevant laws or regulations.
- The preparation of the financial statements in accordance with that framework.
- The inclusion of an adequate description of that framework in the financial statements.

The preparation of the financial statements requires management to exercise judgment in making accounting estimates that are reasonable in the circumstances, as well as to select and apply appropriate accounting policies. These judgments are made in the context of the applicable financial reporting framework.

A4. The financial statements may be prepared in accordance with a financial reporting framework designed to meet:

- The common financial information needs of a wide range of users (that is, “general purpose financial statements”); or
- The financial information needs of specific users (that is, “special purpose financial statements”).

A5. The applicable financial reporting framework often encompasses financial reporting standards established by an authorized or recognized standards setting organization, or legislative or regulatory requirements. In some cases, the financial reporting framework may encompass both financial reporting standards established by an authorized or recognized standards setting organization and legislative or regulatory requirements. Other sources may provide direction on the application of the applicable financial reporting framework. In some cases, the applicable financial reporting framework may encompass such other sources, or may even consist only of such sources. Such other sources may include:

- The legal and ethical environment, including statutes, regulations, court decisions, and professional ethical obligations in relation to accounting matters;
b. Published accounting interpretations of varying authority issued by standards setting, professional or regulatory organizations;
c. Published views of varying authority on emerging accounting issues issued by standards setting, professional or regulatory organizations;
d. General and industry practices widely recognized and prevalent; and
e. Accounting literature.

Where conflicts exist between the financial reporting framework and the sources from which direction on its application may be obtained, or among the sources that encompass the financial reporting framework, the source with the highest authority prevails.

A6. The requirements of the applicable financial reporting framework determine the form and content of the financial statements. Although the framework may not specify how to account for or disclose all transactions or events, it ordinarily embodies sufficient broad principles that can serve as a basis for developing and applying accounting policies that are consistent with the concepts underlying the requirements of the framework.

A7. Some financial reporting frameworks are fair presentation frameworks, while others are compliance frameworks. Financial reporting frameworks that encompass primarily the financial reporting standards established by an organization that is authorized or recognized to promulgate standards to be used by entities for preparing general purpose financial statements are often designed to achieve fair presentation, for example, International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB).

A8. The requirements of the applicable financial reporting framework also determine what constitutes a complete set of financial statements. In the case of many frameworks, financial statements are intended to provide information about the financial position, financial performance and cash flows of an entity. For such frameworks, a complete set of financial statements would include a balance sheet; an income statement; a statement of changes in equity; a cash flow statement; and related notes. For some other financial reporting frameworks, a single financial statement and the related notes might constitute a complete set of financial statements:

- For example, the International Public Sector Accounting Standard (IPSAS), “Financial Reporting under the Cash Basis of Accounting” issued by the International Public Sector Accounting Standards Board.
states that the primary financial statement is a statement of cash receipts and payments when a public sector entity prepares its financial statements in accordance with that IPSAS.

- Other examples of a single financial statement, each of which would include related notes, are:
  - Balance sheet.
  - Statement of income or statement of operations.
  - Statement of retained earnings.
  - Statement of cash flows.
  - Statement of assets and liabilities that does not include owner’s equity.
  - Statement of changes owners’ equity.
  - Statement of revenue and expenses.
  - Statement of operations by product lines.

A9. ISA 210 establishes requirements and provides guidance on determining the acceptability of the applicable financial reporting framework. ISA 800 deals with special considerations when financial statements are prepared in accordance with a special purpose framework.

A10. Because of the significance of the premise to the conduct of an audit, the auditor is required to obtain the agreement of management and, where appropriate, those charged with governance that they acknowledge and understand that they have the responsibilities set out in paragraph A2 as a precondition for accepting the audit engagement.

Considerations Specific to Audits in the Public Sector

A11. The mandates for audits of the financial statements of public sector entities may be broader than those of other entities. As a result, the premise, relating to management’s responsibilities, on which an audit of the financial statements of a public sector entity is conducted may include additional responsibilities, such as the responsibility for the execution of transactions and events in accordance with law, regulation or other authority.

Form of the Auditor’s Opinion (Ref: Para. 8)

A12. The opinion expressed by the auditor is on whether the financial statements are
prepared, in all material respects, in accordance with the applicable financial reporting framework. The form of the auditor’s opinion, however, will depend upon the applicable financial reporting framework and any applicable law or regulation. Most financial reporting frameworks include requirements relating to the presentation of the financial statements; for such frameworks, *preparation* of the financial statements in accordance with the applicable financial reporting framework includes *presentation*.

A13. Where the financial reporting framework is a fair presentation framework, as is generally the case for general purpose financial statements, the opinion required by the ISAs is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view. Where the financial reporting framework is a compliance framework, the opinion required is on whether the financial statements are prepared, in all material respects, in accordance with the framework. Unless specifically stated otherwise, references in the ISAs to the auditor’s opinion cover both forms of opinion.

**Ethical Requirements Relating to an Audit of Financial Statements** (Ref: Para. 14)

A14. The auditor is subject to relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements. Relevant ethical requirements ordinarily comprise Parts A and B of the International Federation of Accountants’ *Code of Ethics for Professional Accountants* (the IFAC Code) related to an audit of financial statements together with national requirements that are more restrictive.

A15. Part A of the IFAC Code establishes the fundamental principles of professional ethics relevant to the auditor when conducting an audit of financial statements and provides a conceptual framework for applying those principles. The fundamental principles with which the auditor is required to comply by the IFAC Code are:

(a) Integrity;
(b) Objectivity;
(c) Professional competence and due care;
(d) Confidentiality; and
(e) Professional behavior.

Part B of the IFAC Code illustrates how the conceptual framework is to be applied in specific situations.

A16. In the case of an audit engagement it is in the public interest and, therefore,
required by the IFAC Code, that the auditor be independent of the entity subject to the audit. The IFAC Code describes independence as comprising both independence of mind and independence in appearance. The auditor’s independence from the entity safeguards the auditor’s ability to form an audit opinion without being affected by influences that might compromise that opinion. Independence enhances the auditor’s ability to act with integrity, to be objective and to maintain an attitude of professional skepticism.

A17. International Standard on Quality Control (ISQC1,113 or national requirements that are at least as demanding,114 deal with the firm’s responsibilities to establish and maintain its system of quality control for audit engagements. ISQC 1 sets out the responsibilities of the firm for establishing policies and procedures designed to provide it with reasonable assurance that the firm and its personnel comply with relevant ethical requirements, including those pertaining to independence.115 ISA 220 sets out the engagement partner’s responsibilities with respect to relevant ethical requirements. These include remaining alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team, determining the appropriate action if matters come to the engagement partner’s attention that indicate that members of the engagement team have not complied with relevant ethical requirements, and forming a conclusion on compliance with independence requirements that apply to the audit engagement.116 ISA 220 recognizes that the engagement team is entitled to rely on a firm’s system of quality control in meeting its responsibilities with respect to quality control procedures applicable to the individual audit engagement, unless information provided by the firm or other parties suggests otherwise.

Professional Skepticism (Ref: Para. 15)

A18. Professional skepticism includes being alert to, for example:

- Audit evidence that contradicts other audit evidence obtained.
- Information that brings into question the reliability of documents and responses to inquiries to be used as audit evidence.
- Conditions that may indicate possible fraud.

113 International Standard on Quality Control (ISQC) 1, “Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements.”
115 ISQC 1, paragraphs 20-25.
116 ISA 220, paragraphs 9-12.
• Circumstances that suggest the need for audit procedures in addition to those required by the ISAs.

A19. Maintaining professional skepticism throughout the audit is necessary if the auditor is, for example, to reduce the risks of:

• Overlooking unusual circumstances.
• Over generalizing when drawing conclusions from audit observations.
• Using inappropriate assumptions in determining the nature, timing, and extent of the audit procedures and evaluating the results thereof.

A20. Professional skepticism is necessary to the critical assessment of audit evidence. This includes questioning contradictory audit evidence and the reliability of documents and responses to inquiries and other information obtained from management and those charged with governance. It also includes consideration of the sufficiency and appropriateness of audit evidence obtained in the light of the circumstances, for example in the case where fraud risk factors exist and a single document, of a nature that is susceptible to fraud, is the sole supporting evidence for a material financial statement amount.

A21. The auditor may accept records and documents as genuine unless the auditor has reason to believe the contrary. Nevertheless, the auditor is required to consider the reliability of information to be used as audit evidence. In cases of doubt about the reliability of information or indications of possible fraud (for example, if conditions identified during the audit cause the auditor to believe that a document may not be authentic or that terms in a document may have been falsified), the ISAs require that the auditor investigate further and determine what modifications or additions to audit procedures are necessary to resolve the matter.

A22. The auditor cannot be expected to disregard past experience of the honesty and integrity of the entity’s management and those charged with governance. Nevertheless, a belief that management and those charged with governance are honest and have integrity does not relieve the auditor of the need to maintain professional skepticism or allow the auditor to be satisfied with less-than-persuasive audit evidence when obtaining reasonable assurance.

**Professional Judgment** (Ref: Para. 16)

A23. Professional judgment is essential to the proper conduct of an audit. This is because interpretation of relevant ethical requirements and the ISAs and the

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118 ISA 240, paragraph 13; ISA 500, paragraph 11; ISA 505, “External Confirmations,” paragraphs 10-11, and 16.
informed decisions required throughout the audit cannot be made without the application of relevant knowledge and experience to the facts and circumstances. Professional judgment is necessary in particular regarding decisions about:

- Materiality and audit risk.
- The nature, timing, and extent of audit procedures used to meet the requirements of the ISAs and gather audit evidence.
- Evaluating whether sufficient appropriate audit evidence has been obtained, and whether more needs to be done to achieve the objectives of the ISAs and thereby, the overall objectives of the auditor.
- The evaluation of management’s judgments in applying the entity’s applicable financial reporting framework.
- The drawing of conclusions based on the audit evidence obtained, for example, assessing the reasonableness of the estimates made by management in preparing the financial statements.

A24. The distinguishing feature of the professional judgment expected of an auditor is that it is exercised by an auditor whose training, knowledge and experience have assisted in developing the necessary competencies to achieve reasonable judgments.

A25. The exercise of professional judgment in any particular case is based on the facts and circumstances that are known by the auditor. Consultation on difficult or contentious matters during the course of the audit, both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm, such as that required by ISA 220,119 assist the auditor in making informed and reasonable judgments.

A26. Professional judgment can be evaluated based on whether the judgment reached reflects a competent application of auditing and accounting principles and is appropriate in the light of, and consistent with, the facts and circumstances that were known to the auditor up to the date of the auditor’s report.

A27. Professional judgment needs to be exercised throughout the audit. It also needs to be appropriately documented. In this regard, the auditor is required to prepare audit documentation sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the significant professional judgments made in reaching conclusions on significant matters arising during the

119ISA 220, paragraph 18.
audit. Professional judgment is not to be used as the justification for decisions that are not otherwise supported by the facts and circumstances of the engagement or sufficient appropriate audit evidence.

**Sufficient Appropriate Audit Evidence and Audit Risk** (Ref: Para. 5 and 17)

*Sufficiency and Appropriateness of Audit Evidence*

A28. Audit evidence is necessary to support the auditor’s opinion and report. It is cumulative in nature and is primarily obtained from audit procedures performed during the course of the audit. It may, however, also include information obtained from other sources such as previous audits (provided the auditor has determined whether changes have occurred since the previous audit that may affect its relevance to the current audit121) or a firm’s quality control procedures for client acceptance and continuance. In addition to other sources inside and outside the entity, the entity’s accounting records are an important source of audit evidence. Also, information that may be used as audit evidence may have been prepared by an expert employed or engaged by the entity. Audit evidence comprises both information that supports and corroborates management’s assertions, and any information that contradicts such assertions. In addition, in some cases, the absence of information (for example, management’s refusal to provide a requested representation) is used by the auditor, and therefore, also constitutes audit evidence. Most of the auditor’s work in forming the auditor’s opinion consists of obtaining and evaluating audit evidence.

A29. The sufficiency and appropriateness of audit evidence are interrelated. Sufficiency is the measure of the quantity of audit evidence. The quantity of audit evidence needed is affected by the auditor’s assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required). Obtaining more audit evidence, however, may not compensate for its poor quality.

A30. Appropriateness is the measure of the quality of audit evidence; that is, its relevance and its reliability in providing support for the conclusions on which the auditor’s opinion is based. The reliability of evidence is influenced by its source and by its nature, and is dependent on the individual circumstances under which it is obtained.

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120ISA 230, paragraph 8.
A31. Whether sufficient appropriate audit evidence has been obtained to reduce audit risk to an acceptably low level, and thereby enable the auditor to draw reasonable conclusions on which to base the auditor’s opinion, is a matter of professional judgment. ISA 500 and other relevant ISAs establish additional requirements and provide further guidance applicable throughout the audit regarding the auditor’s considerations in obtaining sufficient appropriate audit evidence.

Audit Risk

A32. Audit risk is a function of the risks of material misstatement and detection risk. The assessment of risks is based on audit procedures to obtain information necessary for that purpose and evidence obtained throughout the audit. The assessment of risks is a matter of professional judgment, rather than a matter capable of precise measurement.

A33. For purposes of the ISAs, audit risk does not include the risk that the auditor might express an opinion that the financial statements are materially misstated when they are not. This risk is ordinarily insignificant. Further, audit risk is a technical term related to the process of auditing; it does not refer to the auditor’s business risks such as loss from litigation, adverse publicity, or other events arising in connection with the audit of financial statements.

Risks of Material Misstatement

A34. The risks of material misstatement may exist at two levels:

- The overall financial statement level; and
- The assertion level for classes of transactions, account balances, and disclosures.

A35. Risks of material misstatement at the overall financial statement level refer to risks of material misstatement that relate pervasively to the financial statements as a whole and potentially affect many assertions.

A36. Risks of material misstatement at the assertion level are assessed in order to determine the nature, timing, and extent of further audit procedures necessary to obtain sufficient appropriate audit evidence. This evidence enables the auditor to express an opinion on the financial statements at an acceptably low level of audit risk. Auditors use various approaches to accomplish the objective of assessing the risks of material misstatement. For example, the auditor may make use of a model that expresses the general relationship of the components of audit risk in mathematical terms to arrive at an acceptable level of detection risk. Some auditors find such a model to be useful when planning audit procedures.
A37. The risks of material misstatement at the assertion level consist of two components: inherent risk and control risk. Inherent risk and control risk are the entity’s risks; they exist independently of the audit of the financial statements.

A38. Inherent risk is higher for some assertions and related classes of transactions, account balances, and disclosures than for others. For example, it may be higher for complex calculations or for accounts consisting of amounts derived from accounting estimates that are subject to significant estimation uncertainty. External circumstances giving rise to business risks may also influence inherent risk. For example, technological developments might make a particular product obsolete, thereby causing inventory to be more susceptible to overstatement. Factors in the entity and its environment that relate to several or all of the classes of transactions, account balances, or disclosures may also influence the inherent risk related to a specific assertion. Such factors may include, for example, a lack of sufficient working capital to continue operations or a declining industry characterized by a large number of business failures.

A39. Control risk is a function of the effectiveness of the design, implementation and maintenance of internal control by management to address identified risks that threaten the achievement of the entity’s objectives relevant to preparation of the entity’s financial statements. However, internal control, no matter how well designed and operated, can only reduce, but not eliminate, risks of material misstatement in the financial statements, because of the inherent limitations of internal control. These include, for example, the possibility of human errors or mistakes, or of controls being circumvented by collusion or inappropriate management override. Accordingly, some control risk will always exist. The ISAs provide the conditions under which the auditor is required to, or may choose to, test the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures to be performed.122

A40. The ISAs do not ordinarily refer to inherent risk and control risk separately, but rather to a combined assessment of the “risks of material misstatement.” However, the auditor may make separate or combined assessments of inherent and control risk depending on preferred audit techniques or methodologies and practical considerations. The assessment of the risks of material misstatement may be expressed in quantitative terms, such as in percentages, or in non-quantitative terms. In any case, the need for the auditor to make appropriate risk assessments is more important than the different approaches by which they may be made.

122 ISA 330, “The Auditor’s Responses to Assessed Risks,” paragraphs 7-17
A41. ISA 315 establishes requirements and provides guidance on identifying and assessing the risks of material misstatement at the financial statement and assertion levels.

Detection Risk

A42. For a given level of audit risk, the acceptable level of detection risk bears an inverse relationship to the assessed risks of material misstatement at the assertion level. For example, the greater the risks of material misstatement the auditor believes exists, the less the detection risk that can be accepted and, accordingly, the more persuasive the audit evidence required by the auditor.

A43. Detection risk relates to the nature, timing, and extent of the auditor’s procedures that are determined by the auditor to reduce audit risk to an acceptably low level. It is therefore a function of the effectiveness of an audit procedure and of its application by the auditor. Matters such as:

- adequate planning;
- proper assignment of personnel to the engagement team;
- the application of professional skepticism; and
- supervision and review of the audit work performed,

assist to enhance the effectiveness of an audit procedure and of its application and reduce the possibility that an auditor might select an inappropriate audit procedure, misapply an appropriate audit procedure, or misinterpret the audit results.

A44. ISA 300 and ISA 330 establish requirements and provide guidance on planning an audit of financial statements and the auditor’s responses to assessed risks. Detection risk, however, can only be reduced, not eliminated, because of the inherent limitations of an audit. Accordingly, some detection risk will always exist.

Inherent Limitations of an Audit

A45. The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is because there are inherent limitations of an audit, which result in most of the audit evidence on which the auditor draws

\(^{123}\text{ISA 300, “Planning an Audit of Financial Statements.”}\)
conclusions and bases the auditor’s opinion being persuasive rather than conclusive. The inherent limitations of an audit arise from:

- The nature of financial reporting;
- The nature of audit procedures; and
- The need for the audit to be conducted within a reasonable period of time and at a reasonable cost.

The Nature of Financial Reporting

A46. The preparation of financial statements involves judgment by management in applying the requirements of the entity’s applicable financial reporting framework to the facts and circumstances of the entity. In addition, many financial statement items involve subjective decisions or assessments or a degree of uncertainty, and there may be a range of acceptable interpretations or judgments that may be made. Consequently, some financial statement items are subject to an inherent level of variability which cannot be eliminated by the application of additional auditing procedures. For example, this is often the case with respect to certain accounting estimates. Nevertheless, the ISAs require the auditor to give specific consideration to whether accounting estimates are reasonable in the context of the applicable financial reporting framework and related disclosures, and to the qualitative aspects of the entity’s accounting practices, including indicators of possible bias in management’s judgments.\textsuperscript{124}

The Nature of Audit Procedures

A47. There are practical and legal limitations on the auditor’s ability to obtain audit evidence. For example:

- There is the possibility that management or others may not provide, intentionally or unintentionally, the complete information that is relevant to the preparation of the financial statements or that has been requested by the auditor. Accordingly, the auditor cannot be certain of the completeness of information, even though the auditor has performed audit procedures to obtain assurance that all relevant information has been obtained.
- Fraud may involve sophisticated and carefully organized schemes designed to conceal it. Therefore, audit procedures used to gather audit evidence may be ineffective for detecting an intentional misstatement that involves, for example, collusion to falsify documentation which may cause the auditor to believe that

audit evidence is valid when it is not. The auditor is neither trained as nor expected to be an expert in the authentication of documents.

• An audit is not an official investigation into alleged wrongdoing. Accordingly, the auditor is not given specific legal powers, such as the power of search, which may be necessary for such an investigation.

**Timeliness of Financial Reporting and the Balance between Benefit and Cost**

A48. The matter of difficulty, time, or cost involved is not in itself a valid basis for the auditor to omit an audit procedure for which there is no alternative or to be satisfied with audit evidence that is less than persuasive. Appropriate planning assists in making sufficient time and resources available for the conduct of the audit. Notwithstanding this, the relevance of information, and thereby its value, tends to diminish over time, and there is a balance to be struck between the reliability of information and its cost. This is recognized in certain financial reporting frameworks (see, for example, the IASB’s “Framework for the Preparation and Presentation of Financial Statements”). Therefore, there is an expectation by users of financial statements that the auditor will form an opinion on the financial statements within a reasonable period of time and at a reasonable cost, recognizing that it is impracticable to address all information that may exist or to pursue every matter exhaustively on the assumption that information is in error or fraudulent until proved otherwise.

A49. Consequently, it is necessary for the auditor to:

• Plan the audit so that it will be performed in an effective manner;
• Direct audit effort to areas most expected to contain risks of material misstatement, whether due to fraud or error, with correspondingly less effort directed at other areas; and
• Use testing and other means of examining populations for misstatements.

A50. In light of the approaches described in paragraph A49, the ISAs contain requirements for the planning and performance of the audit and require the auditor, among other things, to:

• Have a basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels by performing risk assessment procedures and related activities; and
• Use testing and other means of examining populations in a manner that provides a reasonable basis for the auditor to draw conclusions about the population.

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125 ISA 315, paragraphs 5-10.
Other Matters that Affect the Inherent Limitations of an Audit

A51. In the case of certain assertions or subject matters, the potential effects of the inherent limitations on the auditor’s ability to detect material misstatements are particularly significant. Such assertions or subject matters include:

- Fraud, particularly fraud involving senior management or collusion. See ISA 240 for further discussion.
- The existence and completeness of related party relationships and transactions. See ISA 550 for further discussion.
- The occurrence of non-compliance with laws and regulations. See ISA 250 for further discussion.
- Future events or conditions that may cause an entity to cease to continue as a going concern. See ISA 570 for further discussion.

Relevant ISAs identify specific audit procedures to assist in mitigating the effect of the inherent limitations.

A52. Because of the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with ISAs. Accordingly, the subsequent discovery of a material misstatement of the financial statements resulting from fraud or error does not by itself indicate a failure to conduct an audit in accordance with ISAs. However, the inherent limitations of an audit are not a justification for the auditor to be satisfied with less-than-persuasive audit evidence. Whether the auditor has performed an audit in accordance with ISAs is determined by the audit procedures performed in the circumstances, the sufficiency and appropriateness of the audit evidence obtained as a result thereof and the suitability of the auditor’s report based on an evaluation of that evidence in light of the overall objectives of the auditor.

Conduct of an Audit in Accordance with ISAs

Nature of the ISAs (Ref: Para. 18)

A53. The ISAs, taken together, provide the standards for the auditor’s work in fulfilling

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126 ISA 330; ISA 500; ISA 520, “Analytical Procedures;” ISA 530, “Audit Sampling.”
127 ISA 550, “Related Parties.”
128 ISA 250, “Consideration of Laws and Regulations in an Audit of Financial Statements.”
129 ISA 570, “Going Concern.”
the overall objectives of the auditor. The ISAs deal with the general responsibilities of the auditor, as well as the auditor’s further considerations relevant to the application of those responsibilities to specific topics.

A54. The scope, effective date and any specific limitation of the applicability of a specific ISA is made clear in the ISA. Unless otherwise stated in the ISA, the auditor is permitted to apply an ISA before the effective date specified therein.

A55. In performing an audit, the auditor may be required to comply with legal or regulatory requirements in addition to the ISAs. The ISAs do not override law or regulation that governs an audit of financial statements. In the event that such law or regulation differs from the ISAs, an audit conducted only in accordance with law or regulation will not automatically comply with ISAs.

A56. The auditor may also conduct the audit in accordance with both ISAs and auditing standards of a specific jurisdiction or country. In such cases, in addition to complying with each of the ISAs relevant to the audit, it may be necessary for the auditor to perform additional audit procedures in order to comply with the relevant standards of that jurisdiction or country.

Considerations Specific to Audits in the Public Sector

A57. The ISAs are relevant to engagements in the public sector. The public sector auditor’s responsibilities, however, may be affected by the audit mandate, or by obligations on public sector entities arising from law, regulation or other authority (such as ministerial directives, government policy requirements, or resolutions of the legislature), which may encompass a broader scope than an audit of financial statements in accordance with the ISAs. These additional responsibilities are not dealt with in the ISAs. They may be dealt with in the pronouncements of the International Organization of Supreme Audit Institutions or national standard setters, or in guidance developed by government audit agencies.

Contents of the ISAs (Ref: Para. 19)

A58. In addition to objectives and requirements (requirements are expressed in the ISAs using “shall”), an ISA contains related guidance in the form of application and other explanatory material. It may also contain introductory material that provides context relevant to a proper understanding of the ISA, and definitions. The entire text of an ISA, therefore, is relevant to an understanding of the objectives stated in an ISA and the proper application of the requirements of an ISA.

A59. Where necessary, the application and other explanatory material provides further
explanation of the requirements of an ISA and guidance for carrying them out. In particular, it may:

- Explain more precisely what a requirement means or is intended to cover.
- Include examples of procedures that may be appropriate in the circumstances.

While such guidance does not in itself impose a requirement, it is relevant to the proper application of the requirements of an ISA. The application and other explanatory material may also provide background information on matters addressed in an ISA.

A60. Appendices form part of the application and other explanatory material. The purpose and intended use of an appendix are explained in the body of the related ISA or within the title and introduction of the appendix itself.

A61. Introductory material may include, as needed, such matters as explanation of:

- The purpose and scope of the ISA, including how the ISA relates to other ISAs.
- The subject matter of the ISA.
- The respective responsibilities of the auditor and others in relation to the subject matter of the ISA.
- The context in which the ISA is set.

A62 An ISA may include, in a separate section under the heading “Definitions,” a description of the meanings attributed to certain terms for purposes of the ISAs. These are provided to assist in the consistent application and interpretation of the ISAs, and are not intended to override definitions that may be established for other purposes, whether in law, regulation or otherwise. Unless otherwise indicated, those terms will carry the same meanings throughout the ISAs. The Glossary of Terms relating to International Standards issued by the International Auditing and Assurance Standards Board in the *Handbook of International Standards on Auditing and Quality Control* published by IFAC contains a complete listing of terms defined in the ISAs. It also includes descriptions of other terms found in ISAs to assist in common and consistent interpretation and translation.

A63. When appropriate, additional considerations specific to audits of smaller entities and public sector entities are included within the application and other explanatory material of an ISA. These additional considerations assist in the application of the requirements of the ISA in the audit of such entities. They do
not, however, limit or reduce the responsibility of the auditor to apply and comply with the requirements of the ISAs.

Considerations Specific to Smaller Entities

A64. For purposes of specifying additional considerations to audits of smaller entities, a “smaller entity” refers to an entity which typically possesses qualitative characteristics such as:

(a) Concentration of ownership and management in a small number of individuals (often a single individual – either a natural person or another enterprise that owns the entity provided the owner exhibits the relevant qualitative characteristics); and

(b) One or more of the following:

(i) Straightforward or uncomplicated transactions;

(ii) Simple record-keeping;

(iii) Few lines of business and few products within business lines;

(iv) Few internal controls;

(v) Few levels of management with responsibility for a broad range of controls; or

(vi) Few personnel, many having a wide range of duties.

These qualitative characteristics are not exhaustive, they are not exclusive to smaller entities, and smaller entities do not necessarily display all of these characteristics.

A65. The considerations specific to smaller entities included in the ISAs have been developed primarily with unlisted entities in mind. Some of the considerations, however, may be helpful in audits of smaller listed entities.

A66. The ISAs refer to the proprietor of a smaller entity who is involved in running the entity on a day-to-day basis as the “owner-manager.”

Objectives Stated in Individual ISAs (Ref: Para. 21)

A67. Each ISA contains one or more objectives which provide a link between the requirements and the overall objectives of the auditor. The objectives in individual ISAs serve to focus the auditor on the desired outcome of the ISA, while being specific enough to assist the auditor in:

- Understanding what needs to be accomplished and, where necessary, the appropriate means of doing so; and

- Deciding whether more needs to be done to achieve them in the particular circumstances of the audit.
A68. Objectives are to be understood in the context of the overall objectives of the auditor stated in paragraph 11 of this ISA. As with the overall objectives of the auditor, the ability to achieve an individual objective is equally subject to the inherent limitations of an audit.

A69. In using the objectives, the auditor is required to have regard to the interrelationships among the ISAs. This is because, as indicated in paragraph A53, the ISAs deal in some cases with general responsibilities and in others with the application of those responsibilities to specific topics. For example, this ISA requires the auditor to adopt an attitude of professional skepticism; this is necessary in all aspects of planning and performing an audit but is not repeated as a requirement of each ISA. At a more detailed level, ISA 315 and ISA 330 contain, among other things, objectives and requirements that deal with the auditor’s responsibilities to identify and assess the risks of material misstatement and to design and perform further audit procedures to respond to those assessed risks, respectively; these objectives and requirements apply throughout the audit. An ISA dealing with specific aspects of the audit (for example, ISA 540) may expand on how the objectives and requirements of such ISAs as ISA 315 and ISA 330 are to be applied in relation to the subject of the ISA but does not repeat them. Thus, in achieving the objective stated in ISA 540, the auditor has regard to the objectives and requirements of other relevant ISAs.

Use of Objectives to Determine Need for Additional Audit Procedures (Ref: Para. 21(a))

A70. The requirements of the ISAs are designed to enable the auditor to achieve the objectives specified in the ISAs, and thereby the overall objectives of the auditor. The proper application of the requirements of the ISAs by the auditor is therefore expected to provide a sufficient basis for the auditor’s achievement of the objectives. However, because the circumstances of audit engagements vary widely and all such circumstances cannot be anticipated in the ISAs, the auditor is responsible for determining the audit procedures necessary to fulfill the requirements of the ISAs and to achieve the objectives. In the circumstances of an engagement, there may be particular matters that require the auditor to perform audit procedures in addition to those required by the ISAs to meet the objectives specified in the ISAs.

Use of Objectives to Evaluate Whether Sufficient Appropriate Audit Evidence Has Been Obtained (Ref: Para. 21(b))
A71. The auditor is required to use the objectives to evaluate whether sufficient appropriate audit evidence has been obtained in the context of the overall objectives of the auditor. If as a result the auditor concludes that the audit evidence is not sufficient and appropriate, then the auditor may follow one or more of the following approaches to meeting the requirement of paragraph 21(b):

- Evaluate whether further relevant audit evidence has been, or will be, obtained as a result of complying with other ISAs;
- Extend the work performed in applying one or more requirements; or
- Perform other procedures judged by the auditor to be necessary in the circumstances.

Where none of the above is expected to be practical or possible in the circumstances, the auditor will not be able to obtain sufficient appropriate audit evidence and is required by the ISAs to determine the effect on the auditor’s report or on the auditor’s ability to complete the engagement.

Complying with Relevant Requirements

Relevant Requirements (Ref: Para. 22)

A72. In some cases, an ISA (and therefore all of its requirements) may not be relevant in the circumstances. For example, if an entity does not have an internal audit function, nothing in ISA 610 is relevant.

A73. Within a relevant ISA, there may be conditional requirements. Such a requirement is relevant when the circumstances envisioned in the requirement apply and the condition exists. In general, the conditionality of a requirement will either be explicit or implicit, for example:

- The requirement to modify the auditor’s opinion if there is a limitation of scope represents an explicit conditional requirement.
- The requirement to communicate significant deficiencies in internal control identified during the audit to those charged with governance, which depends on the existence of such identified significant deficiencies; and the requirement to obtain sufficient appropriate audit evidence regarding the presentation and disclosure of segment information in accordance with the applicable financial reporting framework, which depends on that framework requiring or permitting such disclosure, represent implicit conditional requirements.

130 ISA 610, "Using the Work of Internal Auditors."
In some cases, a requirement may be expressed as being conditional on applicable law or regulation. For example, the auditor may be required to withdraw from the audit engagement, *where withdrawal is possible under applicable law or regulation*, or the auditor may be required to do something, *unless prohibited by law or regulation*. Depending on the jurisdiction, the legal or regulatory permission or prohibition may be explicit or implicit.

**Departure from a Requirement (Ref: Para. 23)**

A74. ISA 230 establishes documentation requirements in those exceptional circumstances where the auditor departs from a relevant requirement. The ISAs do not call for compliance with a requirement that is not relevant in the circumstances of the audit.

**Failure to Achieve an Objective (Ref: Para. 24)**

A75. Whether an objective has been achieved is a matter for the auditor’s professional judgment. That judgment takes account of the results of audit procedures performed in complying with the requirements of the ISAs, and the auditor’s evaluation of whether sufficient appropriate audit evidence has been obtained and whether more needs to be done in the particular circumstances of the audit to achieve the objectives stated in the ISAs. Accordingly, circumstances that may give rise to a failure to achieve an objective include those that:

- Prevent the auditor from complying with the relevant requirements of an ISA.
- Result in its not being practicable or possible for the auditor to carry out the additional audit procedures or obtain further audit evidence as determined necessary from the use of the objectives in accordance with paragraph 21, for example due to a limitation in the available audit evidence.

A76. Audit documentation that meets the requirements of ISA 230 and the specific documentation requirements of other relevant ISAs provides evidence of the auditor’s basis for a conclusion about the achievement of the overall objectives of the auditor. While it is unnecessary for the auditor to document separately (as in a checklist, for example) that individual objectives have been achieved, the documentation of a failure to achieve an objective assists the auditor’s evaluation of whether such a failure has prevented the auditor from achieving the overall objectives of the auditor.

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134 ISA 230, paragraph 12.
ISSAI 1210

Agreeing the Terms of Audit Engagements
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Agreeing the Terms of Audit Engagements

Introduction to the ISA

ISA 210 deals with the auditor’s responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance. This includes establishing that certain preconditions for an audit, responsibility for which rests with management and, where appropriate, those charged with governance, are present. ISA 2202 deals with those aspects of engagement acceptance that are within the control of the auditor.

Applicability of the ISA in Public Sector Auditing

P2. ISA 210 is applicable to auditors of public sector entities in their role as auditors of financial statements.

P3. The terms of an audit engagement in the public sector are normally mandated and therefore not subject to requests from, and agreement with, management. Therefore the requirements in the ISA, when applied in the public sector context, are useful in establishing a common, formal understanding of the respective roles and responsibilities of management and the auditor. Since the public sector auditor is normally engaged by and reports to the legislature, agreements often need to be reached with both the legislature and management.

1 All Practice Notes are considered together with ISSAI 1000 “General Introduction to the INTOSAI Financial Audit Guidelines.” 2 ISA 220, “Quality Control for an Audit of Financial Statements.”
International Standard on Auditing

Agreeing the Terms of Audit Engagements

ISA 210
April 2009

International Federation of Accountants
INTRODUCTION

International Standard on Auditing (ISA) 210, “Agreeing the Terms of Audit Engagements” should be read in conjunction with ISA 200 “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing.”
Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the auditor’s responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance. This includes establishing that certain preconditions for an audit, responsibility for which rests with management and, where appropriate, those charged with governance, are present. ISA 220\(^{135}\) deals with those aspects of engagement acceptance that are within the control of the auditor. (Ref: Para. A1)

Objective

3. The objective of the auditor is to accept or continue an audit engagement only when the basis upon which it is to be performed has been agreed, through:

   (a) Establishing whether the preconditions for an audit are present; and
   (b) Confirming that there is a common understanding between the auditor and management and, where appropriate, those charged with governance of the terms of the audit engagement.

Definitions

4. For purposes of the ISAs, the following term has the meaning attributed below:

   Preconditions for an audit – The use by management of an acceptable financial reporting framework in the preparation of the financial statements and the agreement of management and, where appropriate, those charged with governance to the premise\(^{136}\) on which an audit is conducted.

5. For the purposes of this ISA, references to “management” should be read hereafter as “management and, where appropriate, those charged with governance.”

Requirements

Preconditions for an Audit

6. In order to establish whether the preconditions for an audit are present, the auditor shall:

   (a) Determine whether the financial reporting framework to be applied in the preparation of the financial statements is acceptable; and (Ref: Para. A2-A10)

\(^{135}\) ISA 220, “Quality Control for an Audit of Financial Statements.”

(b) Obtain the agreement of management that it acknowledges and understands its responsibility: (Ref: Para. A11-A14, A20)

(i) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation; (Ref: Para. A15)

(ii) For such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and (Ref: Para. A16-A19)

(iii) To provide the auditor with:

(a) Access to all information of which management is aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;

(b) Additional information that the auditor may request from management for the purpose of the audit; and

(c) Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

Limitation on Scope Prior to Audit Engagement Acceptance

7. If management or those charged with governance impose a limitation on the scope of the auditor’s work in the terms of a proposed audit engagement such that the auditor believes the limitation will result in the auditor disclaiming an opinion on the financial statements, the auditor shall not accept such a limited engagement as an audit engagement, unless required by law or regulation to do so.

Other Factors Affecting Audit Engagement Acceptance

8. If the preconditions for an audit are not present, the auditor shall discuss the matter with management. Unless required by law or regulation to do so, the auditor shall not accept the proposed audit engagement:

(a) If the auditor has determined that the financial reporting framework to be applied in the preparation of the financial statements is unacceptable, except as provided in paragraph 19; or

(b) If the agreement referred to in paragraph 6(b) has not been obtained.

Agreement on Audit Engagement Terms

9. The auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate. (Ref: Para. A21)

10. Subject to paragraph 11, the agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include: (Ref: Para. A22-A25)
(a) The objective and scope of the audit of the financial statements;
(b) The responsibilities of the auditor;
(c) The responsibilities of management;
(d) Identification of the applicable financial reporting framework for the preparation of the financial statements; and
(e) Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.

11. If law or regulation prescribes in sufficient detail the terms of the audit engagement referred to in paragraph 10, the auditor need not record them in a written agreement, except for the fact that such law or regulation applies and that management acknowledges and understands its responsibilities as set out in paragraph 6(b). (Ref: Para. A22, A26-A27)

12. If law or regulation prescribes responsibilities of management similar to those described in paragraph 6(b), the auditor may determine that the law or regulation includes responsibilities that, in the auditor’s judgment, are equivalent in effect to those set out in that paragraph. For such responsibilities that are equivalent, the auditor may use the wording of the law or regulation to describe them in the written agreement. For those responsibilities that are not prescribed by law or regulation such that their effect is equivalent, the written agreement shall use the in paragraph 6(b). (Ref: Para. A26)

Recurring Audits

13. On recurring audits, the auditor shall assess whether circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the entity of the existing terms of the audit engagement. (Ref: Para. A28)

Acceptance of a Change in the Terms of the Audit Engagement

14. The auditor shall not agree to a change in the terms of the audit engagement where there is no reasonable justification for doing so. (Ref: Para. A29-A31)

15. If, prior to completing the audit engagement, the auditor is requested to change the audit engagement to an engagement that conveys a lower level of assurance, the auditor shall determine whether there is reasonable justification for doing so. (Ref: Para. A32-A33)

16. If the terms of the audit engagement are changed, the auditor and management shall agree on and record the new terms of the engagement in an engagement letter or other suitable form of written agreement.
17. If the auditor is unable to agree to a change of the terms of the audit engagement and is not permitted by management to continue the original audit engagement, the auditor shall:

   a) Withdraw from the audit engagement where possible under applicable law or regulation; and
   b) Determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners or regulators.

**Additional Considerations in Engagement Acceptance**

*Financial Reporting Standards Supplemented by Law or Regulation*

18. If financial reporting standards established by an authorized or recognized standards setting organization are supplemented by law or regulation, the auditor shall determine whether there are any conflicts between the financial reporting standards and the additional requirements. If such conflicts exist, the auditor shall discuss with management the nature of the additional requirements and shall agree whether:

   (a) The additional requirements can be met through additional disclosures in the financial statements; or
   (b) The description of the applicable financial reporting framework in the financial statements can be amended accordingly.

If neither of the above actions is possible, the auditor shall determine whether it will be necessary to modify the auditor’s opinion in accordance with ISA 705.137 (Ref: Para. A34)

*Financial Reporting Framework Prescribed by Law or Regulation—Other Matters Affecting Acceptance*

19. If the auditor has determined that the financial reporting framework prescribed by law or regulation would be unacceptable but for the fact that it is prescribed by law or regulation, the auditor shall accept the audit engagement only if the following conditions are present: (Ref: Para. A35)

   (a) Management agrees to provide additional disclosures in the financial statements required to avoid the financial statements being misleading; and
   (b) It is recognized in the terms of the audit engagement that:

      (i) The auditor’s report on the financial statements will incorporate an

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137 ISA 705, “Modifications to the Opinion in the Independent Auditor’s Report.”
Emphasis of Matter paragraph, drawing users’ attention to the additional disclosures, in accordance with ISA 706; and
(ii) Unless the auditor is required by law or regulation to express the auditor’s opinion on the financial statements by using the phrases “present fairly, in all material respects,” or “give a true and fair view” in accordance with the applicable financial reporting framework, the auditor’s opinion on the financial statements will not include such phrases.

20. If the conditions outlined in paragraph 19 are not present and the auditor is required by law or regulation to undertake the audit engagement, the auditor shall:
   (a) Evaluate the effect of the misleading nature of the financial statements on the auditor’s report; and
   (b) Include appropriate reference to this matter in the terms of the audit engagement.

Auditor’s Report Prescribed by Law or Regulation

21. In some cases, law or regulation of the relevant jurisdiction prescribes the layout or wording of the auditor’s report in a form or in terms that are significantly different from the requirements of ISAs. In these circumstances, the auditor shall evaluate:
   (a) Whether users might misunderstand the assurance obtained from the audit of the financial statements and, if so,
   (b) Whether additional explanation in the auditor’s report can mitigate possible misunderstanding.139

If the auditor concludes that additional explanation in the auditor’s report cannot mitigate possible misunderstanding, the auditor shall not accept the audit engagement, unless required by law or regulation to do so. An audit conducted in accordance with such law or regulation does not comply with ISAs. Accordingly, the auditor shall not include any reference within the auditor’s report to the audit having been conducted in accordance with ISAs.140 (Ref: Para. A36-A37)

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139ISA 706.
140See also ISA 700, “Forming an Opinion and Reporting on Financial Statements,” paragraph 43.
Application and Other Explanatory Material

Scope of this ISA (Ref: Para. 1)

A1. Assurance engagements, which include audit engagements, may only be accepted when the practitioner considers that relevant ethical requirements such as independence and professional competence will be satisfied, and when the engagement exhibits certain characteristics. The auditor’s responsibilities in respect of ethical requirements in the context of the acceptance of an audit engagement and in so far as they are within the control of the auditor are dealt with in ISA 220. This ISA deals with those matters (or preconditions) that are within the control of the entity and upon which it is necessary for the auditor and the entity’s management to agree.

Preconditions for an Audit

The Financial Reporting Framework (Ref: Para. 6(a))

A2. A condition for acceptance of an assurance engagement is that the criteria referred to in the definition of an assurance engagement are suitable and available to intended users. Criteria are the benchmarks used to evaluate or measure the subject matter including, where relevant, benchmarks for presentation and disclosure. Suitable criteria enable reasonably consistent evaluation or measurement of a subject matter within the context of professional judgment. For purposes of the ISAs, the applicable financial reporting framework provides the criteria the auditor uses to audit the financial statements, including where relevant their fair presentation.

A3. Without an acceptable financial reporting framework, management does not have an appropriate basis for the preparation of the financial statements and the auditor does not have suitable criteria for auditing the financial statements. In many cases the auditor may presume that the applicable financial reporting framework is acceptable, as described in paragraphs A8-A9.

Determining the Acceptability of the Financial Reporting Framework

A4. Factors that are relevant to the auditor’s determination of the acceptability of the financial reporting framework to be applied in the preparation of the financial statements include:

- The nature of the entity (for example, whether it is a business enterprise, a public sector entity or a not for profit organization);

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142. ISA 220, paragraphs 9-11.
• The purpose of the financial statements (for example, whether they are prepared to meet the common financial information needs of a wide range of users or the financial information needs of specific users);

• The nature of the financial statements (for example, whether the financial statements are a complete set of financial statements or a single financial statement); and

• Whether law or regulation prescribes the applicable financial reporting framework.

A5. Many users of financial statements are not in a position to demand financial statements tailored to meet their specific information needs. While all the information needs of specific users cannot be met, there are financial information needs that are common to a wide range of users. Financial statements prepared in accordance with a financial reporting framework designed to meet the common financial information needs of a wide range of users are referred to as general purpose financial statements.

A6. In some cases, the financial statements will be prepared in accordance with a financial reporting framework designed to meet the financial information needs of specific users. Such financial statements are referred to as special purpose financial statements. The financial information needs of the intended users will determine the applicable financial reporting framework in these circumstances. ISA 800 discusses the acceptability of financial reporting frameworks designed to meet the financial information needs of specific users.

A7. Deficiencies in the applicable financial reporting framework that indicate that the framework is not acceptable may be encountered after the audit engagement has been accepted. When use of that framework is prescribed by law or regulation, the requirements of paragraphs 19-20 apply. When use of that framework is not prescribed by law or regulation, management may decide to adopt another framework that is acceptable. When management does so, as required by paragraph 16, new terms of the audit engagement are agreed to reflect the change in the framework as the previously agreed terms will no longer be accurate.

General purpose frameworks

A8. At present, there is no objective and authoritative basis that has been generally recognized globally for judging the acceptability of general purpose frameworks. In the absence of such a basis, financial reporting standards established by

\[544\text{ISA 800, “Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks,” paragraph 8.}\]
organizations that are authorized or recognized to promulgate standards to be used by certain types of entities are presumed to be acceptable for general purpose financial statements prepared by such entities, provided the organizations follow an established and transparent process involving deliberation and consideration of the views of a wide range of stakeholders. Examples of such financial reporting standards include:

- International Financial Reporting Standards (IFRSs) promulgated by the International Accounting Standards Board;
- International Public Sector Accounting Standards (IPSASs) promulgated by the International Public Sector Accounting Standards Board; and
- Accounting principles promulgated by an authorized or recognized standards setting organization in a particular jurisdiction, provided the organization follows an established and transparent process involving deliberation and consideration of the views of a wide range of stakeholders.

These financial reporting standards are often identified as the applicable financial reporting framework in law or regulation governing the preparation of general purpose financial statements.

**Financial reporting frameworks prescribed by law or regulation**

A9. In accordance with paragraph 6(a), the auditor is required to determine whether the financial reporting framework, to be applied in the preparation of the financial statements, is acceptable. In some jurisdictions, law or regulation may prescribe the financial reporting framework to be used in the preparation of general purpose financial statements for certain types of entities. In the absence of indications to the contrary, such a financial reporting framework is presumed to be acceptable for general purpose financial statements prepared by such entities. In the event that the framework is not considered to be acceptable, paragraphs 19-20 apply.

**Jurisdictions that do not have standards setting organizations or prescribed financial reporting frameworks**

A10. When an entity is registered or operating in a jurisdiction that does not have an authorized or recognized standards setting organization, or where use of the financial reporting framework is not prescribed by law or regulation, management identifies a financial reporting framework to be applied in the preparation of the financial statements. Appendix 2 contains guidance on determining the acceptability of financial reporting frameworks in such circumstances.
A11. An audit in accordance with ISAs is conducted on the premise that management has acknowledged and understands that it has the responsibilities set out in paragraph 6(b). In certain jurisdictions, such responsibilities may be specified in law or regulation. In others, there may be little or no legal or regulatory definition of such responsibilities. ISAs do not override law or regulation in such matters. However, the concept of an independent audit requires that the auditor’s role does not involve taking responsibility for the preparation of the financial statements or for the entity’s related internal control, and that the auditor has a reasonable expectation of obtaining the information necessary for the audit in so far as management is able to provide or procure it. Accordingly, the premise is fundamental to the conduct of an independent audit. To avoid misunderstanding, agreement is reached with management that it acknowledges and understands that it has such responsibilities as part of agreeing and recording the terms of the audit engagement in paragraphs 9-12.

A12. The way in which the responsibilities for financial reporting are divided between management and those charged with governance will vary according to the resources and structure of the entity and any relevant law or regulation, and the respective roles of management and those charged with governance within the entity. In most cases, management is responsible for execution while those charged with governance have oversight of management. In some cases, those charged with governance will have, or will assume, responsibility for approving the financial statements or monitoring the entity’s internal control related to financial reporting. In larger or public entities, a subgroup of those charged with governance, such as an audit committee, may be charged with certain oversight responsibilities.

A13. ISA 580 requires the auditor to request management to provide written representations that it has fulfilled certain of its responsibilities. It may therefore be appropriate to make management aware that receipt of such written representations will be expected, together with written representations required by other ISAs and, where necessary, written representations to support other audit evidence relevant to the financial statements or one or more specific assertions in the financial statements.

A14. Where management will not acknowledge its responsibilities, or agree to provide the written representations, the auditor will be unable to obtain sufficient

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145 ISA 200, paragraph A2.
appropriate audit evidence. In such circumstances, it would not be appropriate for the auditor to accept the audit engagement, unless law or regulation requires the auditor to do so. In cases where the auditor is required to accept the audit engagement, the auditor may need to explain to management the importance of these matters, and the implications for the auditor’s report.

Preparation of the Financial Statements (Ref: Para. 6(b)(i))

A15. Most financial reporting frameworks include requirements relating to the presentation of the financial statements; for such frameworks, preparation of the financial statements in accordance with the financial reporting framework includes presentation. In the case of a fair presentation framework the importance of the reporting objective of fair presentation is such that the premise agreed with management includes specific reference to fair presentation, or to the responsibility to ensure that the financial statements will “give a true and fair view” in accordance with the financial reporting framework.

Internal Control (Ref: Para. 6(b)(ii))

A16. Management maintains such internal control as it determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. Internal control, no matter how effective, can provide an entity with only reasonable assurance about achieving the entity’s financial reporting objectives due to the inherent limitations of internal control.

A17. An independent audit conducted in accordance with the ISAs does not act as a substitute for the maintenance of internal control necessary for the preparation of financial statements by management. Accordingly, the auditor is required to obtain the agreement of management that it acknowledges and understands its responsibility for internal control. However, the agreement required by paragraph 6(b)(ii) does not imply that the auditor will find that internal control maintained by management has achieved its purpose or will be free of deficiencies.

A18. It is for management to determine what internal control is necessary to enable the preparation of the financial statements. The term “internal control” encompasses a wide range of activities within components that may be described as the control environment; the entity’s risk assessment process; the information system, including the related business processes relevant to financial reporting, and communication; control activities; and monitoring of controls. This division,

147 ISA 580, paragraph A26.
however, does not necessarily reflect how a particular entity may design, implement and maintain its internal control, or how it may classify any particular component.\textsuperscript{149} An entity’s internal control (in particular, its accounting books and records, or accounting systems) will reflect the needs of management, the complexity of the business, the nature of the risks to which the entity is subject, and relevant laws or regulation.

A19. In some jurisdictions, law or regulation may refer to the responsibility of management for the adequacy of accounting books and records, or accounting systems. In some cases, general practice may assume a distinction between accounting books and records or accounting systems on the one hand, and internal control or controls on the other. As accounting books and records, or accounting systems, are an integral part of internal control as referred to in paragraph A18, no specific reference is made to them in paragraph 6(b)(ii) for the description of the responsibility of management. To avoid misunderstanding, it may be appropriate for the auditor to explain to management the scope of this responsibility.

Considerations Relevant to Smaller Entities (Ref: Para. 6(b))

A20. One of the purposes of agreeing the terms of the audit engagement is to avoid misunderstanding about the respective responsibilities of management and the auditor. For example, when a third party has assisted with the preparation of the financial statements, it may be useful to remind management that the preparation of the financial statements in accordance with the applicable financial reporting framework remains its responsibility.

Agreement on Audit Engagement Terms

Agreeing the Terms of the Audit Engagement (Ref: Para. 9)

A21. The roles of management and those charged with governance in agreeing the terms of the audit engagement for the entity depend on the governance structure of the entity and relevant law or regulation.

Audit Engagement Letter or Other Form of Written Agreement\textsuperscript{150}(Ref: Para. 10-11)

A22. It is in the interests of both the entity and the auditor that the auditor sends an audit engagement letter before the commencement of the audit to help avoid misunderstandings with respect to the audit. In some countries, however, the objective and scope of an audit and the responsibilities of management and of the auditor may be sufficiently established by law, that is, they prescribe the matters

\textsuperscript{149} ISA 315, paragraph A51 and Appendix 1.

\textsuperscript{150} In the paragraphs that follow, any reference to an audit engagement letter is to be taken as a reference to an audit engagement letter or other suitable form of written agreement.
described in paragraph 10. Although in these circumstances paragraph 11 permits the auditor to include in the engagement letter only reference to the fact that relevant law or regulation applies and that management acknowledges and understands its responsibilities as set out in paragraph 6(b), the auditor may nevertheless consider it appropriate to include the matters described in paragraph 10 in an engagement letter for the information of management.

Form and Content of the Audit Engagement Letter

A23. The form and content of the audit engagement letter may vary for each entity. Information included in the audit engagement letter on the auditor’s responsibilities may be based on ISA 200. Paragraphs 6(b) and 12 of this ISA deal with the description of the responsibilities of management. In addition to including the matters required by paragraph 10, an audit engagement letter may make reference to, for example:

- Elaboration of the scope of the audit, including reference to applicable legislation, regulations, ISAs, and ethical and other pronouncements of professional bodies to which the auditor adheres.
- The form of any other communication of results of the audit engagement.
- The fact that because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with ISAs.
- Arrangements regarding the planning and performance of the audit, including the composition of the audit team.
- The expectation that management will provide written representations (see also paragraph A13).
- The agreement of management to make available to the auditor draft financial statements and any accompanying other information in time to allow the auditor to complete the audit in accordance with the proposed timetable.
- The agreement of management to inform the auditor of facts that may affect the financial statements, of which management may become aware during the period from the date of the auditor’s report to the date the financial statements are issued.
- The basis on which fees are computed and any billing arrangements.
- A request for management to acknowledge receipt of the audit engagement letter and to agree to the terms of the engagement outlined therein.

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151ISA 200, paragraphs 3-9.
A24. When relevant, the following points could also be made in the audit engagement letter:

- Arrangements concerning the involvement of other auditors and experts in some aspects of the audit.
- Arrangements concerning the involvement of internal auditors and other staff of the entity.
- Arrangements to be made with the predecessor auditor, if any, in the case of an initial audit.
- Any restriction of the auditor’s liability when such possibility exists.
- A reference to any further agreements between the auditor and the entity.
- Any obligations to provide audit working papers to other parties.

An example of an audit engagement letter is set out in Appendix 1.

Audits of Components

A25. When the auditor of a parent entity is also the auditor of a component, the factors that may influence the decision whether to send a separate audit engagement letter to the component include the following:

- Who appoints the component auditor;
- Whether a separate auditor’s report is to be issued on the component;
- Legal requirements in relation to audit appointments;
- Degree of ownership by parent; and
- Degree of independence of the component management from the parent entity.

Responsibilities of Management Prescribed by Law or Regulation (Ref: Para. 11-12)

A26. If, in the circumstances described in paragraphs A22 and A27, the auditor concludes that it is not necessary to record certain terms of the audit engagement in an audit engagement letter, the auditor is still required by paragraph 11 to seek the written agreement from management that it acknowledges and understands that it has the responsibilities set out in paragraph 6(b). However, in accordance with paragraph 12, such written agreement may use the wording of the law or regulation if such law or regulation establishes responsibilities for management that are equivalent in effect to those described in paragraph 6(b). The accounting profession, audit standards setter, or audit regulator in a jurisdiction may have provided guidance as to whether the description in law or regulation is equivalent.
Considerations specific to public sector entities

A27. Law or regulation governing the operations of public sector audits generally mandate the appointment of a public sector auditor and commonly set out the public sector auditor’s responsibilities and powers, including the power to access an entity’s records and other information. When law or regulation prescribes in sufficient detail the terms of the audit engagement, the public sector auditor may nonetheless consider that there are benefits in issuing a fuller audit engagement letter than permitted by paragraph 11.

Recurring Audits (Ref: Para. 13)

A28. The auditor may decide not to send a new audit engagement letter or other written agreement each period. However, the following factors may make it appropriate to revise the terms of the audit engagement or to remind the entity of existing terms:

- Any indication that the entity misunderstands the objective and scope of the audit.
- Any revised or special terms of the audit engagement.
- A recent change of senior management.
- A significant change in ownership.
- A significant change in nature or size of the entity’s business.
- A change in legal or regulatory requirements.
- A change in the financial reporting framework adopted in the preparation of the financial statements.
- A change in other reporting requirements.

Acceptance of a Change in the Terms of the Audit Engagement

Request to Change the Terms of the Audit Engagement (Ref: Para. 14)

A29. A request from the entity for the auditor to change the terms of the audit engagement may result from a change in circumstances affecting the need for the service, a misunderstanding as to the nature of an audit as originally requested or a restriction on the scope of the audit engagement, whether imposed by management or caused by other circumstances. The auditor, as required by paragraph 14, considers the justification given for the request, particularly the implications of a restriction on the scope of the audit engagement.

A30. A change in circumstances that affects the entity’s requirements or a misunderstanding concerning the nature of the service originally requested may be considered a reasonable basis for requesting a change in the audit engagement.
A31. In contrast, a change may not be considered reasonable if it appears that the change relates to information that is incorrect, incomplete or otherwise unsatisfactory. An example might be where the auditor is unable to obtain sufficient appropriate audit evidence regarding receivables and the entity asks for the audit engagement to be changed to a review engagement to avoid a qualified opinion or a disclaimer of opinion.

Request to Change to a Review or a Related Service (Ref: Para. 15)

A32. Before agreeing to change an audit engagement to a review or a related service, an auditor who was engaged to perform an audit in accordance with ISAs may need to assess, in addition to the matters referred to in paragraphs A29- A31 above, any legal or contractual implications of the change.

A33. If the auditor concludes that there is reasonable justification to change the audit engagement to a review or a related service, the audit work performed to the date of change may be relevant to the changed engagement; however, the work required to be performed and the report to be issued would be those appropriate to the revised engagement. In order to avoid confusing the reader, the report on the related service would not include reference to:

(a) The original audit engagement; or

(b) Any procedures that may have been performed in the original audit engagement, except where the audit engagement is changed to an engagement to undertake agreed-upon procedures and thus reference to the procedures performed is a normal part of the report.

Additional Considerations in Engagement Acceptance

Financial Reporting Standards Supplemented by Law or Regulation (Ref: Para. 18)

A34. In some jurisdictions, law or regulation may supplement the financial reporting standards established by an authorized or recognized standards setting organization with additional requirements relating to the preparation of financial statements. In those jurisdictions, the applicable financial reporting framework for the purposes of applying the ISAs encompasses both the identified financial reporting framework and such additional requirements provided they do not conflict with the identified financial reporting framework. This may, for example, be the case when law or regulation prescribes disclosures in addition to those required by the financial reporting standards or when they narrow the range of acceptable choices that can be made within the financial reporting standards.152
Financial Reporting Framework Prescribed by Law or Regulation—Other Matters Affecting Acceptance (Ref: Para. 19)

A35. Law or regulation may prescribe that the wording of the auditor’s opinion use the phrases “present fairly, in all material respects” or “give a true and fair view” in a case where the auditor concludes that the applicable financial reporting framework prescribed by law or regulation would otherwise have been unacceptable. In this case, the terms of the prescribed wording of the auditor’s report are significantly different from the requirements of ISAs (see paragraph 21).

Auditor’s Report Prescribed by Law or Regulation (Ref: Para. 21)

A36. ISAs require that the auditor shall not represent compliance with ISAs unless the auditor has complied with all of the ISAs relevant to the audit. When law or regulation prescribes the layout or wording of the auditor’s report in a form or in terms that are significantly different from the requirements of ISAs and the auditor concludes that additional explanation in the auditor’s report cannot mitigate possible misunderstanding, the auditor may consider including a statement in the auditor’s report that the audit is not conducted in accordance with ISAs. The auditor is, however, encouraged to apply ISAs, including the ISAs that address the auditor’s report, to the extent practicable, notwithstanding that the auditor is not permitted to refer to the audit being conducted in accordance with ISAs.

Considerations Specific to Public Sector Entities

A37. In the public sector, specific requirements may exist within the legislation governing the audit mandate; for example, the auditor may be required to report directly to a minister, the legislature or the public if the entity attempts to limit the scope of the audit.

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152 ISA 700, paragraph 15, includes a requirement regarding the evaluation of whether the financial statements adequately refer to or describe the applicable financial reporting framework.

153 ISA 200, paragraph 20.
Appendix 1

Example of an Audit Engagement Letter

The following is an example of an audit engagement letter for an audit of general purpose financial statements prepared in accordance with International Financial Reporting Standards. This letter is not authoritative but is intended only to be a guide that may be used in conjunction with the considerations outlined in this ISA. It will need to be varied according to individual requirements and circumstances. It is drafted to refer to the audit of financial statements for a single reporting period and would require adaptation if intended or expected to apply to recurring audits (see paragraph 13 of this ISA). It may be appropriate to seek legal advice that any proposed letter is suitable.

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To the appropriate representative of management or those charged with governance of ABC Company:154

[The objective and scope of the audit]

You155 have requested that we audit the financial statements of ABC Company, which comprise the balance sheet as at December 31, 20X1, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information. We are pleased to confirm our acceptance and our understanding of this audit engagement by means of this letter. Our audit will be conducted with the objective of our expressing an opinion on the financial statements.

[The responsibilities of the auditor]

We will conduct our audit in accordance with International Standards on Auditing (ISAs). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial

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154The addressees and references in the letter would be those that are appropriate in the circumstances of the engagement, including the relevant jurisdiction. It is important to refer to the appropriate persons – see paragraph A21.

155Throughout this letter, references to “you,” “we,” “us,” “management,” “those charged with governance” and “auditor” would be used or amended as appropriate in the circumstances.
statements are free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

Because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with ISAs.

In making our risk assessments, we consider internal control relevant to the entity’s preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. However, we will communicate to you in writing concerning any significant deficiencies in internal control relevant to the audit of the financial statements that we have identified during the audit.

[The responsibilities of management and identification of the applicable financial reporting framework (for purposes of this example it is assumed that the auditor has not determined that the law or regulation prescribes those responsibilities in appropriate terms; the descriptions in paragraph 6(b) of this ISA are therefore used).]

Our audit will be conducted on the basis that [management and, where appropriate, those charged with governance156 acknowledge and understand that they have responsibility:

(a) For the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards;157

(b) For such internal control as [management] determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and

156 Use terminology as appropriate in the circumstances.
157 Or, if appropriate, “For the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards.”
(c) To provide us with:
   (i) Access to all information of which [management] is aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
   (ii) Additional information that we may request from [management] for the purpose of the audit; and
   (iii) Unrestricted access to persons within the entity from whom we determine it necessary to obtain audit evidence.

As part of our audit process, we will request from [management and, where appropriate, those charged with governance], written confirmation concerning representations made to us in connection with the audit.

We look forward to full cooperation from your staff during our audit. [Other relevant information]

[Insert other information, such as fee arrangements, billings and other specific terms, as appropriate.]

[Reporting]

[Insert appropriate reference to the expected form and content of the auditor’s report.]

The form and content of our report may need to be amended in the light of our audit findings.

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our audit of the financial statements including our respective responsibilities.

XYZ & Co.

Acknowledged and agreed on behalf of ABC Company by

(signed)

........................
Name and Title
Date
Determining the Acceptability of General Purpose Frameworks

Jurisdictions that Do Not Have Authorized or Recognized Standards Setting Organizations or Financial Reporting Frameworks Prescribed by Law or Regulation

1. As explained in paragraph A10 of this ISA, when an entity is registered or operating in a jurisdiction that does not have an authorized or recognized standards setting organization, or where use of the financial reporting framework is not prescribed by law or regulation, management identifies an applicable financial reporting framework. Practice in such jurisdictions is often to use the financial reporting standards established by one of the organizations described in paragraph A8 of this ISA.

2. Alternatively, there may be established accounting conventions in a particular jurisdiction that are generally recognized as the financial reporting framework for general purpose financial statements prepared by certain specified entities operating in that jurisdiction. When such a financial reporting framework is adopted, the auditor is required by paragraph 6(a) of this ISA to determine whether the accounting conventions collectively can be considered to constitute an acceptable financial reporting framework for general purpose financial statements. When the accounting conventions are widely used in a particular jurisdiction, the accounting profession in that jurisdiction may have considered the acceptability of the financial reporting framework on behalf of the auditors. Alternatively, the auditor may make this determination by considering whether the accounting conventions exhibit attributes normally exhibited by acceptable financial reporting frameworks (see paragraph 3 below), or by comparing the accounting conventions to the requirements of an existing financial reporting framework considered to be acceptable (see paragraph 4 below).

3. Acceptable financial reporting frameworks normally exhibit the following attributes that result in information provided in financial statements that is useful to the intended users:

   (a) Relevance, in that the information provided in the financial statements is relevant to the nature of the entity and the purpose of the financial statements.
For example, in the case of a business enterprise that prepares general purpose financial statements, relevance is assessed in terms of the information necessary to meet the common financial information needs of a wide range of users in making economic decisions. These needs are ordinarily met by presenting the financial position, financial performance and cash flows of the business enterprise.

(b) Completeness, in that transactions and events, account balances and disclosures that could affect conclusions based on the financial statements are not omitted.

(c) Reliability, in that the information provided in the financial statements:
   (i) Where applicable, reflects the economic substance of events and transactions and not merely their legal form; and
   (ii) Results in reasonably consistent evaluation, measurement, presentation and disclosure, when used in similar circumstances.

(d) Neutrality, in that it contributes to information in the financial statements that is free from bias.

(e) Understandability, in that the information in the financial statements is clear and comprehensive and not subject to significantly different interpretation.

4. The auditor may decide to compare the accounting conventions to the requirements of an existing financial reporting framework considered to be acceptable. For example, the auditor may compare the accounting conventions to IFRSs. For an audit of a small entity, the auditor may decide to compare the accounting conventions to a financial reporting framework specifically developed for such entities by an authorized or recognized standards setting organization. When the auditor makes such a comparison and differences are identified, the decision as to whether the accounting conventions adopted in the preparation of the financial statements constitute an acceptable financial reporting framework includes considering the reasons for the differences and whether application of conventions, or the description of the financial reporting framework in the financial statements, could result in financial statements that are misleading.

5. A conglomeration of accounting conventions devised to suit individual preferences is not an acceptable financial reporting framework for general purpose financial statements. Similarly, a compliance framework will not be an acceptable financial reporting framework, unless it is generally accepted in the particular jurisdictions by preparers and users.
ISSAI 1220

Quality Control for an Audit of Financial Statements

The International Standards of Supreme Audit Institutions, ISSAI, are issued by the International Organization of Supreme Audit Institutions, INTOSAI. For more information visit www.issai.org.
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Quality Control for an Audit of Financial Statements

Introduction to the ISA

ISA 220 deals with the specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements. It also addresses, where applicable, the responsibilities of the engagement quality control reviewer. The ISA is to be read in conjunction with relevant ethical requirements.

Applicability of the ISA in Public Sector Auditing

P2. ISA 220 is applicable to auditors of public sector entities in their role as auditors of financial statements.
International Standard on Auditing

Quality Control for an Audit of Financial Statements

International Federation of Accountants
## INTERNATIONAL STANDARD ON AUDITING 220
### QUALITY CONTROL FOR AN AUDIT OF FINANCIAL STATEMENTS
(Effective for audits of financial statements for periods beginning on or after December 15, 2009)

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Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements. It also addresses, where applicable, the responsibilities of the engagement quality control reviewer. This ISA is to be read in conjunction with relevant ethical requirements.

Objective

2. The objective of the auditor is to implement quality control procedures at the engagement level that provide the auditor with reasonable assurance that:

   (a) The audit complies with professional standards and applicable legal and regulatory requirements; and
   
   (b) The auditor’s report issued is appropriate in the circumstances.

Definitions

7. For purposes of the ISAs, the following terms have the meanings attributed below:

   (a) Engagement partner\textsuperscript{159} – The partner or other person in the firm who is responsible for the audit engagement and its performance, and for the auditor’s report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.

   (b) Engagement quality control review – A process designed to provide an objective evaluation, on or before the date of the auditor’s report, of the significant judgments the engagement team made and the conclusions it reached in formulating the auditor’s report. The engagement quality control review process is only for audits of financial statements of listed entities and those other audit engagements, if any, for which the firm has determined an engagement quality control review, is required.

   (c) Engagement quality control reviewer – A partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, none of whom is part of the engagement team, with sufficient and appropriate experience and authority to objectively evaluate the significant judgments the engagement team made and the conclusions it reached in formulating the auditor’s report.

\textsuperscript{158}ISQC 1, “Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements,” paragraph 11.

\textsuperscript{159}“Engagement partner,” “partner,” and “firm” should be read as referring to their public sector equivalents where relevant.
(d) Engagement team—All partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform audit procedures on the engagement. This excludes an auditor’s external expert engaged by the firm or a network firm.\textsuperscript{160}

(e) Firm—A sole practitioner, partnership or corporation or other entity of professional accountants.

(f) Inspection—In relation to completed audit engagements, procedures designed to provide evidence of compliance by engagement teams with the firm’s quality control policies and procedures.

(g) Listed entity—An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body.

(h) Monitoring—A process comprising an ongoing consideration and evaluation of the firm’s system of quality control, including a periodic inspection of a selection of completed engagements, designed to provide the firm with reasonable assurance that its system of quality control is operating effectively.

(i) Network firm—A firm or entity that belongs to a network.

(j) Network—A larger structure:
   (i) That is aimed at cooperation, and
   (ii) That is clearly aimed at profit or cost-sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.

(k) Partner—Any individual with authority to bind the firm with respect to the performance of a professional services engagement.

(l) Personnel—Partners and staff.

(m) Professional standards—International Standards on Auditing (ISAs) and relevant ethical requirements.

(n) Relevant ethical requirements—Ethical requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Parts A and B of the International Federation of Accountants’ \textit{Code of Ethics for Professional Accountants} (IFAC Code) related to an audit of financial statements together with national requirements that are more restrictive.

(o) Staff—Professionals, other than partners, including any experts the firm employs.

\textsuperscript{160} ISA 620, “Using the Work of an Auditor’s Expert,” paragraph 6(a), defines the term “auditor’s expert.”
Suitably qualified external person – An individual outside the firm with the competence and capabilities to act as an engagement partner, for example a partner of another firm, or an employee (with appropriate experience) of either a professional accountancy body whose members may perform audits of historical financial information or of an organization that provides relevant quality control services.

Requirements

Leadership Responsibilities for Quality on Audits
8. The engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned. (Ref: Para. A3)

Relevant Ethical Requirements
9. Throughout the audit engagement, the engagement partner shall remain alert, through observation and making inquiries as necessary, for evidence of non-compliance with relevant ethical requirements by members of the engagement team. (Ref: Para. A4-A5)
10. If matters come to the engagement partner’s attention through the firm’s system of quality control or otherwise that indicate that members of the engagement team have not complied with relevant ethical requirements, the engagement partner, in consultation with others in the firm, shall determine the appropriate action. (Ref: Para. A5)

Independence
11. The engagement partner shall form a conclusion on compliance with independence requirements that apply to the audit engagement. In doing so, the engagement partner shall: (Ref: Para. A5)
   (a) Obtain relevant information from the firm and, where applicable, network firms, to identify and evaluate circumstances and relationships that create threats to independence;
   (b) Evaluate information on identified breaches, if any, of the firm’s independence policies and procedures to determine whether they create a threat to independence for the audit engagement; and
   (c) Take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the audit engagement, where withdrawal is possible under applicable law or regulation. The engagement partner shall promptly report to the firm any inability to resolve the matter for appropriate action. (Ref: Para. A6-A7)
Acceptance and Continuance of Client Relationships and Audit Engagements

12. The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed, and shall determine that conclusions reached in this regard are appropriate. (Ref: Para. A8-A9)

13. If the engagement partner obtains information that would have caused the firm to decline the audit engagement had that information been available earlier, the engagement partner shall communicate that information promptly to the firm, so that the firm and the engagement partner can take the necessary action. (Ref: Para. A9)

Assignment of Engagement Teams

14. The engagement partner shall be satisfied that the engagement team, and any auditor’s experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to:

   (a) Perform the audit engagement in accordance with professional standards and applicable legal and regulatory requirements; and
   (b) Enable an auditor’s report that is appropriate in the circumstances to be issued. (Ref: Para. A10-A12)

Engagement Performance

Direction, Supervision and Performance

15. The engagement partner shall take responsibility for:

   (a) The direction, supervision and performance of the audit engagement in compliance with professional standards and applicable legal and regulatory requirements; and (Ref: Para. A13-A15, A20)
   (b) The auditor’s report being appropriate in the circumstances.

Reviews

16. The engagement partner shall take responsibility for reviews being performed in accordance with the firm’s review policies and procedures. (Ref: Para. A16-A17, A20)

17. On or before the date of the auditor’s report, the engagement partner shall, through a review of the audit documentation and discussion with the engagement team, be satisfied that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the auditor’s report to be issued. (Ref: Para. A18-A20)
Consultation

18. The engagement partner shall:

(a) Take responsibility for the engagement team undertaking appropriate consultation on difficult or contentious matters;

(b) Be satisfied that members of the engagement team have undertaken appropriate consultation during the course of the engagement, both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm;

(c) Be satisfied that the nature and scope of, and conclusions resulting from, such consultations are agreed with the party consulted; and

(d) Determine that conclusions resulting from such consultations have been implemented. (Ref: Para. A21-A22)

Engagement Quality Control Review

19. For audits of financial statements of listed entities, and those other audit engagements, if any, for which the firm has determined that an engagement quality control review is required, the engagement partner shall:

(a) Determine that an engagement quality control reviewer has been appointed;

(b) Discuss significant matters arising during the audit engagement, including those identified during the engagement quality control review, with the engagement quality control reviewer; and

(c) Not date the auditor’s report until the completion of the engagement quality control review. (Ref: Para. A23-A25)

20. The engagement quality control reviewer shall perform an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor’s report. This evaluation shall involve:

(a) Discussion of significant matters with the engagement partner;

(b) Review of the financial statements and the proposed auditor’s report;

(c) Review of selected audit documentation relating to the significant judgments the engagement team made and the conclusions it reached; and

(d) Evaluation of the conclusions reached in formulating the auditor’s report and consideration of whether the proposed auditor’s report is appropriate. (Ref: Para. A26-A27, A29-A31)

21. For audits of financial statements of listed entities, the engagement quality control reviewer, on performing an engagement quality control review, shall also consider
the following:

(a) The engagement team’s evaluation of the firm’s independence in relation to the audit engagement;

(b) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; and

(c) Whether audit documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached. (Ref: Para. A28-A31)

**Differences of Opinion**

22. If differences of opinion arise within the engagement team, with those consulted or, where applicable, between the engagement partner and the engagement quality control reviewer, the engagement team shall follow the firm’s policies and procedures for dealing with and resolving differences of opinion.

**Monitoring**

23. An effective system of quality control includes a monitoring process designed to provide the firm with reasonable assurance that its policies and procedures relating to the system of quality control are relevant, adequate, and operating effectively. The engagement partner shall consider the results of the firm’s monitoring process as evidenced in the latest information circulated by the firm and, if applicable, other network firms and whether deficiencies noted in that information may affect the audit engagement. (Ref: Para A32-A34).

**Documentation**

24. The auditor shall include in the audit documentation:

25. The engagement quality control reviewer shall document, for the audit engagement reviewed, that:

(a) The procedures required by the firm’s policies on engagement quality control review have been performed;

(b) The engagement quality control review has been completed on or before the date of the auditor’s report; and

(c) The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the engagement team made and the conclusions it reached were not appropriate.

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Application and Other Explanatory Material

System of Quality Control and Role of Engagement Teams (Ref: Para. 2)

A1. ISQC 1, or national requirements that are at least as demanding, deals with the firm’s responsibilities to establish and maintain its system of quality control for audit engagements. The system of quality control includes policies and procedures that address each of the following elements:

- Leadership responsibilities for quality within the firm;
- Relevant ethical requirements;
- Acceptance and continuance of client relationships and specific engagements;
- Human resources;
- Engagement performance; and
- Monitoring.

National requirements that deal with the firm’s responsibilities to establish and maintain a system of quality control are at least as demanding as ISQC 1 when they address all the elements referred to in this paragraph and impose obligations on the firm that achieve the aims of the requirements set out in ISQC 1.

Reliance on the Firm’s System of Quality Control (Ref: Para. 4)

A2. Unless information provided by the firm or other parties suggest otherwise, the engagement team may rely on the firm’s system of quality control in relation to, for example:

- Competence of personnel through their recruitment and formal training.
- Independence through the accumulation and communication of relevant independence information.
- Maintenance of client relationships through acceptance and continuance systems.
- Adherence to applicable legal and regulatory requirements through the monitoring process.

Leadership Responsibilities for Quality on Audits (Ref: Para. 8)

A3. The actions of the engagement partner and appropriate messages to the other members of the engagement team, in taking responsibility for the overall quality on each audit engagement, emphasize:

(a) The importance to audit quality of:
(i) Performing work that complies with professional standards and applicable legal and regulatory requirements;
(ii) Complying with the firm’s quality control policies and procedures as applicable;
(iii) Issuing auditor’s reports that are appropriate in the circumstances; and
(iv) The engagement team’s ability to raise concerns without fear of reprisals; and
(b) The fact that quality is essential in performing audit engagements.

**Relevant Ethical Requirements**

*Compliance with Relevant Ethical Requirements* (Ref: Para. 9)

A4. The IFAC Code establishes the fundamental principles of professional ethics, which include:

- (a) Integrity;
- (b) Objectivity;
- (c) Professional competence and due care;
- (d) Confidentiality; and
- (e) Professional behavior.

**Definition of “Firm,” “Network” and “Network Firm”** (Ref: Para. 9-11)

A5. The definitions of “firm,” “network” or “network firm” in relevant ethical requirements may differ from those set out in this ISA. For example, the IFAC Code defines the “firm” as:

- (a) A sole practitioner, partnership or corporation of professional accountants;
- (b) An entity that controls such parties through ownership, management or other means; and
- (c) An entity controlled by such parties through ownership, management or other means.

The IFAC Code also provides guidance in relation to the terms “network” and “network firm.”

In complying with the requirements in paragraphs 9-11, the definitions used in the relevant ethical requirements apply in so far as is necessary to interpret those ethical requirements.

**Threats to Independence** (Ref: Para. 11(c))

A6. The engagement partner may identify a threat to independence regarding the audit engagement that safeguards may not be able to eliminate or reduce to an acceptable level. In that case, as required by paragraph 11(c), the engagement
partner reports to the relevant person(s) within the firm to determine appropriate action, which may include eliminating the activity or interest that creates the threat, or withdrawing from the audit engagement, where withdrawal is possible under applicable law or regulation.

Considerations Specific to Public Sector Entities

A7. Statutory measures may provide safeguards for the independence of public sector auditors. However, public sector auditors or audit firms carrying out public sector audits on behalf of the statutory auditor may, depending on the terms of the mandate in a particular jurisdiction, need to adapt their approach in order to promote compliance with the spirit of paragraph 11. This may include, where the public sector auditor’s mandate does not permit withdrawal from the engagement, disclosure through a public report, of circumstances that have arisen that would, if they were in the private sector, lead the auditor to withdraw.

Acceptance and Continuance of Client Relationships and Audit Engagements (Ref: Para. 12)

A8. ISQC 1 requires the firm to obtain information considered necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. Information such as the following assists the engagement partner in determining whether the conclusions reached regarding the acceptance and continuance of client relationships and audit engagements are appropriate:

- The integrity of the principal owners, key management and those charged with governance of the entity;
- Whether the engagement team is competent to perform the audit engagement and has the necessary capabilities, including time and resources;
- Whether the firm and the engagement team can comply with relevant ethical requirements; and
- Significant matters that have arisen during the current or previous audit engagement, and their implications for continuing the relationship.

Considerations Specific to Public Sector Entities (Ref: Para. 12-13)

A9. In the public sector, auditors may be appointed in accordance with statutory procedures. Accordingly, certain of the requirements and considerations regarding
the acceptance and continuance of client relationships and audit engagements as set out in paragraphs 12, 13 and A8 may not be relevant. Nonetheless, information gathered as a result of the process described may be valuable to public sector auditors in performing risk assessments and in carrying out reporting responsibilities.

**Assignment of Engagement Teams** (Ref: Para. 14)

A10. An engagement team includes a person using expertise in a specialized area of accounting or auditing, whether engaged or employed by the firm, if any, who performs audit procedures on the engagement. However, a person with such expertise is not a member of the engagement team if that person’s involvement with the engagement is only consultation. Consultations are addressed in paragraph 18, and paragraph A21-A22.

A11. When considering the appropriate competence and capabilities expected of the engagement team as a whole, the engagement partner may take into consideration such matters as the teams:

- Understanding of, and practical experience with, audit engagements of a similar nature and complexity through appropriate training and participation.
- Understanding of professional standards and applicable legal and regulatory requirements.
- Technical expertise, including expertise with relevant information technology and specialized areas of accounting or auditing.
- Knowledge of relevant industries in which the client operates.
- Ability to apply professional judgment.
- Understanding of the firm’s quality control policies and procedures.

**Considerations Specific to Public Sector Entities**

A12. In the public sector, additional appropriate competence may include skills that are necessary to discharge the terms of the audit mandate in a particular jurisdiction. Such competence may include an understanding of the applicable reporting arrangements, including reporting to the legislature or other governing body or in the public interest. The wider scope of a public sector audit may include, for example, some aspects of performance auditing or a comprehensive assessment of compliance with law, regulation or other authority and preventing and detecting fraud and corruption.
Engagement Performance

Direction, Supervision and Performance (Ref: Para. 15(a))

A13. Direction of the engagement team involves informing the members of the engagement team of matters such as:

- Their responsibilities, including the need to comply with relevant ethical requirements, and to plan and perform an audit with professional skepticism as required by ISA 200.\(^\text{163}\)
- Responsibilities of respective partners where more than one partner is involved in the conduct of an audit engagement.
- The objectives of the work to be performed.
- The nature of the entity’s business.
- Risk-related issues.
- Problems that may arise.
- The detailed approach to the performance of the engagement.

Discussion among members of the engagement team allows less experienced team members to raise questions with more experienced team members so that appropriate communication can occur within the engagement team.

A14. Appropriate teamwork and training assist less experienced members of the engagement team to clearly understand the objectives of the assigned work.

A15. Supervision includes matters such as:

- Tracking the progress of the audit engagement.
- Considering the competence and capabilities of individual members of the engagement team, including whether they have sufficient time to carry out their work, whether they understand their instructions, and whether the work is being carried out in accordance with the planned approach to the audit engagement.
- Addressing significant matters arising during the audit engagement, considering their significance and modifying the planned approach appropriately.
- Identifying matters for consultation or consideration by more experienced engagement team members during the audit engagement.

Reviews

Review Responsibilities (Ref: Para. 16)

A16. Under ISQC 1, the firm’s review responsibility policies and procedures are determined on the basis that work of less experienced team members is reviewed by more experienced team members.164

A17. A review consists of consideration whether, for example:
   a. The work has been performed in accordance with professional standards and applicable legal and regulatory requirements;
   b. Significant matters have been raised for further consideration;
   c. Appropriate consultations have taken place and the resulting conclusions have been documented and implemented;
   d. There is a need to revise the nature, timing and extent of work performed;
   e. The work performed supports the conclusions reached and is appropriately documented;
   f. The evidence obtained is sufficient and appropriate to support the auditor’s report; and
   g. The objectives of the engagement procedures have been achieved.

The Engagement Partner’s Review of Work Performed (Ref: Para. 17)

A18. Timely reviews of the following by the engagement partner at appropriate stages during the engagement allow significant matters to be resolved on a timely basis to the engagement partner’s satisfaction on or before the date of the auditor’s report:
   1. Critical areas of judgment, especially those relating to difficult or contentious matters identified during the course of the engagement;
   2. Significant risks; and
   3. Other areas the engagement partner considers important.

The engagement partner need not review all audit documentation, but may do so. However, as required by ISA 230, the partner documents the extent and timing of there views.165

A19. An engagement partner taking over an audit during the engagement may apply the review procedures as described in paragraphs A18 to review the work performed

164ISQC 1, paragraph 33.
165ISA 230, paragraph 9(c).
to the date of a change in order to assume the responsibilities of an engagement partner.

*Considerations Relevant Where a Member of the Engagement Team with Expertise in a Specialized Area of Accounting or Auditing Is Used* (Ref: Para. 15-17)

A20. Where a member of the engagement team with expertise in a specialized area of accounting or auditing is used, direction, supervision and review of that engagement team member’s work may include matters such as:

a. Agreeing with that member the nature, scope and objectives of that member’s work; and the respective roles of, and the nature, timing and extent of communication between that member and other members of the engagement team.

b. Evaluating the adequacy of that member’s work including the relevance and reasonableness of that member’s findings or conclusions and their consistency with other audit evidence.

*Consultation* (Ref: Para. 18)

A21. Effective consultation on significant technical, ethical, and other matters within the firm or, where applicable, outside the firm can be achieved when those consulted:

- Are given all the relevant facts that will enable them to provide informed advice; and
- Have appropriate knowledge, seniority and experience.

A22. It may be appropriate for the engagement team to consult outside the firm, for example, where the firm lacks appropriate internal resources. They may take advantage of advisory services provided by other firms, professional and regulatory bodies, or commercial organizations that provide relevant quality control services.

*Engagement Quality Control Review*

Completion of the Engagement Quality Control Review before Dating of the Auditor’s Report (Ref: Para. 19(c))

A23. ISA 700 requires the auditor’s report to be dated no earlier than the date on which the auditor has obtained sufficient appropriate evidence on which to base the
auditor’s opinion on the financial statements.\textsuperscript{166} In cases of an audit of financial statements of listed entities or when an engagement meets the criteria for an engagement quality control review, such a review assists the auditor in determining whether sufficient appropriate evidence has been obtained.

A24. Conducting the engagement quality control review in a timely manner at appropriate stages during the engagement allows significant matters to be promptly resolved to the engagement quality control reviewer’s satisfaction on or before the date of the auditor’s report.

A25. Completion of the engagement quality control review means the completion by the engagement quality control reviewer of the requirements in paragraphs 20-21, and where applicable, compliance with paragraph 22. Documentation of the engagement quality control review may be completed after the date of the auditor’s report as part of the assembly of the final audit file. ISA 230 establishes requirements and provides guidance in this regard.\textsuperscript{167}

Nature, Extent and Timing of Engagement Quality Control Review (Ref: Para. 20)

A26. Remaining alert for changes in circumstances allows the engagement partner to identify situations in which an engagement quality control review is necessary, even though at the start of the engagement, such a review was not required.

A27. The extent of the engagement quality control review may depend, among other things, on the complexity of the audit engagement, whether the entity is a listed entity, and the risk that the auditor’s report might not be appropriate in the circumstances. The performance of an engagement quality control review does not reduce the responsibilities of the engagement partner for the audit engagement and its performance.

Engagement Quality Control Review of Listed Entities (Ref: Para. 21)

A28. Other matters relevant to evaluating the significant judgments made by the engagement team that may be considered in an engagement quality control review of a listed entity include:

- Significant risks identified during the engagement in accordance with ISA 315,\textsuperscript{168} and the responses to those risks in accordance with ISA 330,\textsuperscript{169}

\textsuperscript{166}ISA 700, “Forming an Opinion and Reporting on Financial Statements,” paragraph 41.
\textsuperscript{167}ISA 230, paragraphs 14-16.
\textsuperscript{168}ISA 315, “Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment.”
\textsuperscript{169}ISA 330, “The Auditor’s Responses to Assessed Risks.”
including the engagement team’s assessment of, and response to, the risk of fraud in accordance with ISA 240.170

- Judgments made, particularly with respect to materiality and significant risks.
- The significance and disposition of corrected and uncorrected misstatements identified during the audit.
- The matters to be communicated to management and those charged with governance and, where applicable, other parties such as regulatory bodies.

These other matters, depending on the circumstances, may also be applicable for engagement quality control reviews for audits of financial statements of other entities.

Considerations Specific to Smaller Entities (Ref: Para. 20-21)

A29. In addition to the audits of financial statements of listed entities, an engagement quality control review is required for audit engagements that meet the criteria established by the firm that subjects engagements to an engagement quality control review. In some cases, none of the firm’s audit engagements may meet the criteria that would subject them to such a review.

Considerations Specific to Public Sector Entities (Ref: Para. 20-21)

A30. In the public sector, a statutorily appointed auditor (for example, an Auditor General, or other suitably qualified person appointed on behalf of the Auditor General), may act in a role equivalent to that of engagement partner with overall responsibility for public sector audits. In such circumstances, where applicable, the selection of the engagement quality control reviewer includes consideration of the need for independence from the audited entity and the ability of the engagement quality control reviewer to provide an objective evaluation.

A31. Listed entities as referred to in paragraphs 21 and A28 are not common in the public sector. However, there may be other public sector entities that are significant due to size, complexity or public interest aspects, and which consequently have a wide range of stakeholders. Examples include state owned corporations and public utilities. Ongoing transformations within the public sector may also give rise to new types of significant entities. There are no fixed objective criteria on which the determination of significance is based. Nonetheless, public sector auditors evaluate which entities may be of sufficient significance to warrant performance of an engagement quality control review.

**Monitoring** (Ref: Para. 23)

A32. ISQC 1 requires the firm to establish a monitoring process designed to provide it with reasonable assurance that the policies and procedures relating to the system of quality control are relevant, adequate and operating effectively.\(^{171}\)

A33. In considering deficiencies that may affect the audit engagement, the engagement partner may have regard to measures the firm took to rectify the situation that the engagement partner considers are sufficient in the context of that audit.

A34. A deficiency in the firm’s system of quality control does not necessarily indicate that a particular audit engagement was not performed in accordance with professional standards and applicable legal and regulatory requirements, or that the auditor’s report was not appropriate.

**Documentation**

*Documentation of Consultations* (Ref: Para. 24(d))

A35. Documentation of consultations with other professionals that involve difficult or contentious matters that is sufficiently complete and detailed contributes to an understanding of:

- The issue on which consultation was sought; and
- The results of the consultation, including any decisions taken, the basis for those decisions and how they were implemented.

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\(^{171}\)ISQC 1, paragraph 48
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Audit Documentation

Introduction to the ISA

ISA 230 deals with the auditor’s responsibility to prepare audit documentation for an audit of financial statements. The Appendix in the ISA lists other ISAs that contain specific documentation requirements and guidance. The specific documentation requirements of other ISAs do not limit the application of this ISA. Law or regulation may establish additional documentation requirements.

Applicability of the ISA in Public Sector Auditing

P2. ISA 230 is applicable to auditors of public sector entities in their role as auditors of financial statements.
# INTERNATIONAL STANDARD ON AUDITING 230
## AUDIT DOCUMENTATION
(Effective for audits of financial statements for periods beginning on or after December 15, 2009)

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Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the auditor’s responsibility to prepare audit documentation for an audit of financial statements. The Appendix lists other ISAs that contain specific documentation requirements and guidance. The specific documentation requirements of other ISAs do not limit the application of this ISA. Law or regulation may establish additional documentation requirements.

Nature and Purposes of Audit Documentation

2. Audit documentation that meets the requirements of this ISA and the specific documentation requirements of other relevant ISAs provides:

   (a) Evidence of the auditor’s basis for a conclusion about the achievement of the overall objectives of the auditor\(^ {172}\); and
   (b) Evidence that the audit was planned and performed in accordance with ISAs and applicable legal and regulatory requirements.

3. Audit documentation serves a number of additional purposes, including the following:

   • Assisting the engagement team to plan and perform the audit.
   • Assisting members of the engagement team responsible for supervision to direct and supervise the audit work, and to discharge their review responsibilities in accordance with ISA 220\(^ {173}\).
   • Enabling the engagement team to be accountable for its work.
   • Retaining a record of matters of continuing significance to future audits.
   • Enabling the conduct of quality control reviews and inspections in accordance with ISQC 1\(^ {174}\) or national requirements that are at least as demanding\(^ {175}\).
   • Enabling the conduct of external inspections in accordance with applicable legal, regulatory or other requirements.


\(^{174}\)ISQC 1, “Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance

\(^{175}\)ISA 220, paragraph 2.
Objective

5. The objective of the auditor is to prepare documentation that provides:
   (a) A sufficient and appropriate record of the basis for the auditor’s report; and
   (b) Evidence that the audit was planned and performed in accordance with ISAs and applicable legal and regulatory requirements.

Definitions

6. For purposes of the ISAs, the following terms have the meanings attributed below:
   (a) Audit documentation – The record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached (terms such as “working papers” or “work papers” are also sometimes used).
   (b) Audit file – One or more folders or other storage media, in physical or electronic form, containing the records that comprise the audit documentation for a specific engagement.
   (c) Experienced auditor – An individual (whether internal or external to the firm) who has practical audit experience, and a reasonable understanding of:
      i. Audit processes;
      ii. ISAs and applicable legal and regulatory requirements;
      iii. The business environment in which the entity operates; and
      iv. Auditing and financial reporting issues relevant to the entity’s industry.

Requirements

Timely Preparation of Audit Documentation

7. The auditor shall prepare audit documentation on a timely basis. (Ref: Para. A1)
Documentation of the Audit Procedures Performed and Audit Evidence Obtained

Form, Content and Extent of Audit Documentation

8. The auditor shall prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand: (Ref: Para. A2-A5, A16-A17)
   (a) The nature, timing and extent of the audit procedures performed to comply with the ISAs and applicable legal and regulatory requirements; (Ref: Para. A6-A7)
   (b) The results of the audit procedures performed, and the audit evidence obtained; and
   (c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions. (Ref: Para. A8-A11)

9. In documenting the nature, timing and extent of audit procedures performed, the auditor shall record:
   (a) The identifying characteristics of the specific items or matters tested; (Ref: Para. A12)
   (b) Who performed the audit work and the date such work was completed; and
   (c) Who reviewed the audit work performed and the date and extent of such review (Ref: Para. A13)

10. The auditor shall document discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place. (Ref: Para. A14)

11. If the auditor identified information that is inconsistent with the auditor’s final conclusion regarding a significant matter, the auditor shall document how the auditor addressed the inconsistency. (Ref: Para. A15)

Departure from a Relevant Requirement

12. If, in exceptional circumstances, the auditor judges it necessary to depart from a relevant requirement in an ISA, the auditor shall document how the alternative audit procedures performed achieve the aim of that requirement, and the reasons for the departure. (Ref: Para. A18-A19)
Matters Arising after the Date of the Auditor’s Report

13. If, in exceptional circumstances, the auditor performs new or additional audit procedures or draws new conclusions after the date of the auditor’s report, the auditor shall document: (Ref: Para. A20)

   (a) The circumstances encountered;

   (b) The new or additional audit procedures performed, audit evidence obtained, and conclusions reached, and their effect on the auditor’s report; and

   (c) When and by whom the resulting changes to audit documentation were made and reviewed.

Assembly of the Final Audit File

14. The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor’s report. (Ref: Para. A21-A22)

15. After the assembly of the final audit file has been completed, the auditor shall not delete or discard audit documentation of any nature before the end of its retention period. (Ref: Para. A23)

16. In circumstances other than those envisaged in paragraph 13 where the auditor finds it necessary to modify existing audit documentation or add new audit documentation after the assembly of the final audit file has been completed, the auditor shall, regardless of the nature of the modifications or additions, document: (Ref: Para. A24)

   (a) The specific reasons for making them; and

   (b) When and by whom they were made and reviewed.
Application and Other Explanatory Material

Timely Preparation of Audit Documentation (Ref: Para. 7)

A1. Preparing sufficient and appropriate audit documentation on a timely basis helps to enhance the quality of the audit and facilitates the effective review and evaluation of the audit evidence obtained and conclusions reached before the auditor’s report is finalized. Documentation prepared after the audit work has been performed is likely to be less accurate than documentation prepared at the time such work is performed.

Documentation of the Audit Procedures Performed and Audit Evidence Obtained

Form, Content and Extent of Audit Documentation (Ref: Para. 8)

A2. The form, content and extent of audit documentation depend on factors such as:

- The size and complexity of the entity.
- The nature of the audit procedures to be performed.
- The identified risks of material misstatement.
- The significance of the audit evidence obtained.
- The nature and extent of exceptions identified.
- The need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained.
- The audit methodology and tools used.

A3. Audit documentation may be recorded on paper or on electronic or other media. Examples of audit documentation include:

- Audit programs.
- Analyses.
- Issues memoranda.
- Summaries of significant matters.
- Letters of confirmation and representation.
- Checklists.
- Correspondence (including e-mail) concerning significant matters.
The auditor may include abstracts or copies of the entity’s records (for example, significant and specific contracts and agreements) as part of audit documentation. Audit documentation, however, is not a substitute for the entity’s accounting records.

A4. The auditor need not include in audit documentation superseded drafts of working papers and financial statements, notes that reflect incomplete or preliminary thinking, previous copies of documents corrected for typographical or other errors, and duplicates of documents.

A5. Oral explanations by the auditor, on their own, do not represent adequate support for the work the auditor performed or conclusions the auditor reached, but may be used to explain or clarify information contained in the audit documentation.

**Documentation of Compliance with ISAs (Ref: Para. 8(a))**

A6. In principle, compliance with the requirements of this ISA will result in the audit documentation being sufficient and appropriate in the circumstances. Other ISAs contain specific documentation requirements that are intended to clarify the application of this ISA in the particular circumstances of those other ISAs. The specific documentation requirements of other ISAs do not limit the application of this ISA. Furthermore, the absence of a documentation requirement in any particular ISA is not intended to suggest that there is no documentation that will be prepared as a result of complying with that ISA.

A7. Audit documentation provides evidence that the audit complies with the ISAs. However, it is neither necessary nor practicable for the auditor to document every matter considered, or professional judgment made, in an audit. Further, it is unnecessary for the auditor to document separately (as in a checklist, for example) compliance with matters for which compliance is demonstrated by documents included within the audit file. For example:

- The existence of an adequately documented audit plan demonstrates that the auditor has planned the audit.

- The existence of a signed engagement letter in the audit file demonstrates that the auditor has agreed the terms of the audit engagement with management or, where appropriate, those charged with governance.

- An auditor’s report containing an appropriately qualified opinion on the financial statements demonstrates that the auditor has complied with the requirement to express a qualified opinion under the circumstances specified in the ISAs.
• In relation to requirements that apply generally throughout the audit, there may be a number of ways in which compliance with them may be demonstrated within the audit file:

  o For example, there may be no single way in which the auditor’s professional skepticism is documented. But the audit documentation may nevertheless provide evidence of the auditor’s exercise of professional skepticism in accordance with the ISAs. Such evidence may include specific procedures performed to corroborate management’s responses to the auditor’s inquiries.

  o Similarly, that the engagement partner has taken responsibility for the direction, supervision and performance of the audit in compliance with the ISAs may be evidenced in a number of ways within the audit documentation. This may include documentation of the engagement partner’s timely involvement in aspects of the audit, such as participation in the team discussions required by ISA 315\(^{176}\).

Documentation of Significant Matters and Related Significant Professional Judgments (Ref: Para. 8(c))

A8. Judging the significance of a matter requires an objective analysis of the facts and circumstances. Examples of significant matters include:

  • Matters that give rise to significant risks (as defined in ISA 315).

  • Results of audit procedures indicating (a) that the financial statements could be materially misstated, or (b) a need to revise the auditor’s previous assessment of the risks of material misstatement and the auditor’s responses to those risks.

  • Circumstances that cause the auditor significant difficulty in applying necessary audit procedures.

  • Findings that could result in a modification to the audit opinion or the inclusion of an Emphasis of Matter paragraph in the auditor’s report.

A9. An important factor in determining the form, content and extent of audit documentation of significant matters is the extent of professional judgment exercised in performing the work and evaluating the results. Documentation of the professional judgments made, where significant, serves to explain the auditor’s conclusions and to reinforce the quality of the judgment. Such matters are of particular interest to those responsible for reviewing audit documentation,

including those carrying out subsequent audits when reviewing matters of continuing significance (for example, when performing a retrospective review of accounting estimates).

A10. Some examples of circumstances in which, in accordance with paragraph 8, it is appropriate to prepare audit documentation relating to the use of professional judgment include, where the matters and judgments are significant:

- The rationale for the auditor’s conclusion when a requirement provides that the auditor “shall consider” certain information or factors, and that consideration is significant in the context of the particular engagement.

- The basis for the auditor’s conclusion on the reasonableness of areas of subjective judgments (for example, the reasonableness of significant accounting estimates).

- The basis for the auditor’s conclusions about the authenticity of a document when further investigation (such as making appropriate use of an expert or of confirmation procedures) is undertaken in response to conditions identified during the audit that caused the auditor to believe that the document may not be authentic.

A11. The auditor may consider it helpful to prepare and retain as part of the audit documentation a summary (sometimes known as a completion memorandum) that describes the significant matters identified during the audit and how they were addressed, or that includes cross-references to other relevant supporting audit documentation that provides such information. Such a summary may facilitate effective and efficient reviews and inspections of the audit documentation, particularly for large and complex audits. Further, the preparation of such a summary may assist the auditor’s consideration of the significant matters. It may also help the auditor to consider whether, in light of the audit procedures performed and conclusions reached, there is any individual relevant ISA objective that the auditor cannot achieve that would prevent the auditor from achieving the overall objectives of the auditor.

Identification of Specific Items or Matters Tested, and of the Preparer and Reviewer (Ref: Para. 9)

A12. Recording the identifying characteristics serves a number of purposes. For example, it enables the engagement team to be accountable for its work and facilitates the investigation of exceptions or inconsistencies. Identifying characteristics will vary with the nature of the audit procedure and the item or matter tested. For example:

- For a detailed test of entity-generated purchase orders, the auditor may identify the documents selected for testing by their dates and unique purchase order numbers.
For a procedure requiring selection or review of all items over a specific amount from a given population, the auditor may record the scope of the procedure and identify the population (for example, all journal entries over a specified amount from the journal register).

For a procedure requiring systematic sampling from a population of documents, the auditor may identify the documents selected by recording their source, the starting point and the sampling interval (for example, a systematic sample of shipping reports selected from the shipping log for the period from April 1 to September 30, starting with report number 12345 and selecting every 125th report).

For a procedure requiring inquiries of specific entity personnel, the auditor may record the dates of the inquiries and the names and job designations of the entity personnel.

For an observation procedure, the auditor may record the process or matter being observed, the relevant individuals, their respective responsibilities, and where and when the observation was carried out.

A13. ISA 220 requires the auditor to review the audit work performed through review of the audit documentation. The requirement to document who reviewed the audit work performed does not imply a need for each specific working paper to include evidence of review. The requirement, however, means documenting what audit work was reviewed, who reviewed such work, and when it was reviewed.

Documentation of Discussions of Significant Matters with Management, Those Charged with Governance, and Others (Ref: Para. 10)

A14. The documentation is not limited to records prepared by the auditor but may include other appropriate records such as minutes of meetings prepared by the entity’s personnel and agreed by the auditor. Others with whom the auditor may discuss significant matters may include other personnel within the entity, and external parties, such as persons providing professional advice to the entity.

Documentation of How Inconsistencies have been addressed (Ref: Para. 11)

A15. The requirement to document how the auditor addressed inconsistencies in information does not imply that the auditor needs to retain documentation that is incorrect or superseded.

Considerations Specific to Smaller Entities (Ref. Para. 8)

A16. The audit documentation for the audit of a smaller entity is generally less extensive than that for the audit of a larger entity. Further, in the case of an audit where the engagement partner performs all the audit work, the documentation will not include matters that might have to be documented solely to inform or
instruct members of an engagement team, or to provide evidence of review by other members of the team (for example, there will be no matters to document relating to team discussions or supervision). Nevertheless, the engagement partner complies with the overriding requirement in paragraph 8 to prepare audit documentation that can be understood by an experienced auditor, as the audit documentation may be subject to review by external parties for regulatory or other purposes.

A17. When preparing audit documentation, the auditor of a smaller entity may also find it helpful and efficient to record various aspects of the audit together in a single document, with cross-references to supporting working papers as appropriate. Examples of matters that may be documented together in the audit of a smaller entity include the understanding of the entity and its internal control, the overall audit strategy and audit plan, materiality determined in accordance with ISA 320, assessed risks, significant matters noted during the audit, and conclusions reached.

Departure from a Relevant Requirement (Ref: Para. 12)

A18. The requirements of the ISAs are designed to enable the auditor to achieve the objectives specified in the ISAs, and thereby the overall objectives of the auditor. Accordingly, other than in exceptional circumstances, the ISAs call for compliance with each requirement that is relevant in the circumstances of the audit.

A19. The documentation requirement applies only to requirements that are relevant in the circumstances. A requirement is not relevant only in the cases where:

- The entire ISA is not relevant (for example, if an entity does not have an internal audit function, nothing in ISA 610 is relevant); or
- The requirement is conditional and the condition does not exist (for example, the requirement to modify the auditor’s opinion where there is an inability to obtain sufficient appropriate audit evidence, and there is no such inability).

Matters Arising after the Date of the Auditor’s Report (Ref: Para. 13)

A20. Examples of exceptional circumstances include facts which become known to the auditor after the date of the auditor’s report but which existed at that date and which if known at that date, might have caused the financial statements to be amended or the auditor to modify the opinion in the auditor’s report.\(^{177}\) The resulting changes to the audit documentation are reviewed in accordance with the

\(^{177}\)ISA 560, “Subsequent Events,” paragraph 14
review responsibilities set out in ISA 220\textsuperscript{178}, with the engagement partner taking final responsibility for the changes.

**Assembly of the Final Audit File (Ref: Para. 14-16)**

A21. ISQC 1 (or national requirements that are at least as demanding) requires firms to establish policies and procedures for the timely completion of the assembly of audit files.\textsuperscript{179} An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than 60 days after the date of the auditor’s report\textsuperscript{180}.

A22. The completion of the assembly of the final audit file after the date of the auditor’s report is an administrative process that does not involve the performance of new audit procedures or the drawing of new conclusions. Changes may, however, be made to the audit documentation during the final assembly process if they are administrative in nature. Examples of such changes include:

- Deleting or discarding superseded documentation.
- Sorting, collating and cross-referencing working papers.
- Signing off on completion checklists relating to the file assembly process.
- Documenting audit evidence that the auditor has obtained, discussed and agreed with the relevant members of the engagement team before the date of the auditor’s report.

A23. ISQC 1 (or national requirements that are at least as demanding) requires firms to establish policies and procedures for the retention of engagement documentation.\textsuperscript{181} The retention period for audit engagements ordinarily is no shorter than five years from the date of the auditor’s report, or, if later, the date of the group auditor’s report\textsuperscript{182}.

A24. An example of a circumstance in which the auditor may find it necessary to modify existing audit documentation or add new audit documentation after file assembly has been completed is the need to clarify existing audit documentation arising from comments received during monitoring inspections performed by internal or external parties.

\textsuperscript{178}ISQC 1, paragraph 45
\textsuperscript{179}ISQC 1, paragraph 45
\textsuperscript{180}ISQC 1, paragraph A54.
\textsuperscript{181}ISQC 1, paragraph 47.
\textsuperscript{182}ISQC 1, paragraph A61.