

ISSAI4000

Compliance Audit Standard



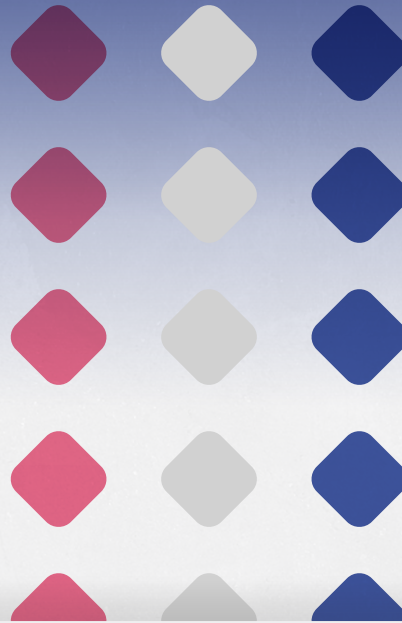
INTOSAI

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by the International
Organisation of Supreme Audit
Institutions, INTOSAI, as part of
the INTOSAI Framework of
Professional Pronouncements.

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INTOSAI



INTOSAI, 2019

- 1) Endorsed as Compliance Audit Guidelines – General Introduction in 2010
- 2) Revised and endorsed as Compliance Audit Standard in 2016
- 3) With the establishment of the Intosai Framework of Professional Pronouncements (IFPP), editorial changes were made in 2019

ISSAI 4000 is available in all INTOSAI official languages: Arabic, English, French, German and Spanish

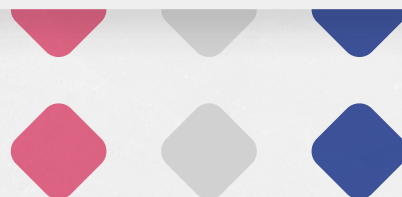


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- 1) Professional standards and guidelines are essential for the credibility, transparency, quality and professionalism of public-sector auditing. *The Compliance Audit Standard (ISSAI 4000)* developed by the International Organisation of Supreme Audit Institutions (INTOSAI) aims 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) Professional standards have a dual purpose: to provide a benchmark for public sector auditing and to enhance the stakeholders¹ confidence in the conclusion(s) in reports.
- 3) *ISSAI 100 - Fundamental Principles of Public-Sector Auditing* defines the purpose and authority of ISSAIs and the framework for public sector auditing. *ISSAI 400 - Compliance Audit Principles* builds on and further develops the fundamental principles of ISSAI 100 to suit the specific context of compliance auditing.
- 4) ISSAI 4000 is based on the fundamental principles for public sector auditing in ISSAI 100 and compliance audit principles in ISSAI 400.
- 5) Compliance audit is a separate audit type. However, some of the principles are to some extent influenced by or shared with both financial and performance audit. ISSAI 4000 refers to the ISSAI 2000-series and *ISSAI 3000 Performance Audit Standard* as appropriate.

1 The term stakeholder is defined in this document as in *INTOSAI-P 12 - The Value and Benefits of Supreme Audit Institutions* – making a difference to the lives of citizens /3; a person, group, organization, member or system that can affect or can be affected by the actions, objectives and policies of government and public sector entities

- 6) ISSAI 4000 contains mandatory requirements and explanations. Requirements contain the minimum necessary for high quality audit work. Requirements are “shall” statements presented in bold, while explanations elaborate the requirement in detail.
- 7) ISSAI 4000 uses the term ‘the auditor’ with the same meaning as in ISSAI 100². Where it is relevant – e.g. where institutional issues are involved - reference is also made to the Supreme Audit Institution (‘the SAI’).
- 8) ISSAI 4000 is structured largely in the same order as ISSAI 400 and consists of four sections:
 - a) The first section establishes the authority of the *Compliance Audit Standards* and how Supreme Audit Institutions (SAIs) can refer to them in their audit reports.
 - b) The second section defines compliance auditing and its objectives, as well as the principles underlying the concept of compliance.
 - c) The third section consists of general requirements for compliance auditing. These requirements shall be considered prior to commencement and throughout the audit process.
 - d) The fourth section contains requirements related to the main stages of the audit process itself.

2

SCOPE OF THIS ISSAI

- 9) The ISSAI 4000 will in no way override national laws, regulations or mandates or prevent SAIs from carrying out investigations or other engagements that are not specifically covered.
- 10) This document provides the International Standard for Compliance Auditing. According to ISSAI 400/2–9, SAIs wishing to make reference to the ISSAI framework relating to compliance auditing can do so in two ways:
 - a) Option 1: by developing authoritative standards that are based on or consistent with the Compliance Audit Principles, or
 - b) Option 2: by adopting the International Standards of Supreme Audit Institutions on Compliance Auditing (ISSAI 4000-4899).
- 11) Under Option 1, INTOSAI recognises that SAIs have various mandates and work under different conditions. Due to the varied situations and structural arrangements of SAIs, not all auditing standards or guidelines may apply to all aspects of their work. National standards can achieve the principles of ISSAI 400 in different ways, given the national mandate, constitutional and other legal environment or the strategy of the SAI.
- 12) SAIs have the option of developing authoritative standards that are consistent with ISSAI 100 and ISSAI 400. If a SAI chooses to develop its own national standards, those standards should include the level of detail necessary to accomplish the SAI's relevant audit functions and should correspond to ISSAI 100 and ISSAI 400 in all applicable and relevant aspects.

- 13) SAIs should declare which standard they apply when conducting audits and this declaration should be accessible to user(s) of the SAI's reports. SAIs should make reference to the standard they follow in their audit reports; however, a more general form of communication may be used covering a defined range of engagements. Meaning that the SAI can state in their reports that they follow international standards without mentioning each individual standard used for each report. This is to make the reports more user friendly.
- 14) Under Option 2, the auditor and the SAI shall comply with each requirement of the ISSAI 4000, unless the requirement is not relevant. If all relevant requirements have not been fulfilled, reference to ISSAI 4000 shall not be made without disclosure of that fact and further explanations about the consequences thereof.
- 15) When a SAI chooses to make reference to ISSAI 4000, the reference should be formulated in accordance with the principles defined by ISSAI 100/10–12 and ISSAI 400/9. Compliance audits may be conducted either as a stand-alone engagement in accordance with ISSAI 4000, or combined with financial or performance audit.
- 16) For combined audits, the auditor assesses which standard to refer to. When a compliance audit is combined with a financial audit, the conclusion/opinion on the aspect of compliance should be clearly separated from the opinion on the financial statements. The identified applicable law(s) and regulation(s) should contain all laws and regulations that can influence the outcomes (=amounts) of the financial transactions that are (or should be) accounted for in the financial statements.
- 17) The requirements and explanations of ISSAI 4000 apply to compliance audits as a stand-alone engagement or a component of a financial or a performance audit engagement.
- 18) According to their mandate, SAIs may also perform tasks that are not considered to be assurance engagements. These tasks are not covered by this ISSAI and therefore the SAI will have to refer to other standards or requirements for the work performed.

3

THE THREE PARTIES IN COMPLIANCE AUDITING

- 19) Public sector audits involve three separate parties: the responsible party, the auditor and the intended user(s).
- a) The responsible party is the executive branch of central or local government and/or its underlying hierarchy of public officials and entities responsible for the management of public funds and/or the exercise of authority under the control of the legislature. The responsible party in compliance auditing is responsible for the subject matter or the subject matter information of the audit.³
 - b) The auditor aims to obtain sufficient and appropriate audit evidence in order to arrive at a conclusion to enhance the degree of confidence of the intended user(s), other than the responsible party, about the measurement or evaluation of a subject matter against criteria.⁴
 - c) The intended user(s) are the persons for whom the auditor prepares the compliance audit report. The intended user(s) may be legislative or oversight bodies, those charged with governance, the public prosecutor or the general public. While the audit report is not addressed to the responsible party, the result can be useful in the improvement of their performance.⁵

3 ISSAI 400/37.

4 ISSAI 400/35.

5 ISSAI 400/38.

COMPLIANCE AUDITS CONDUCTED BY SAIS WITH JURISDICTIONAL POWERS

- 20) SAIs with jurisdictional powers have the authority to exercise judgment and make decisions concerning public officials responsible for non-compliant accounts. These SAIs have the authority to enforce sanctions. In doing so the SAIs comply with the basic principles of the rule of law. Some SAIs are mandated to refer facts liable to criminal prosecution to the judicial authorities. For these SAIs there may be national requirements in addition to the requirements in this ISSAI.
- 21) SAIs with jurisdictional powers may also pronounce judgments and sanctions on those responsible for managing public funds and assets. Such SAIs may assess whether responsible persons may be held liable for the loss, misuse or waste of public funds or assets and whether they ought to be subject to sanctions or penalties.
- 22) SAIs with jurisdictional powers follow the audit process as it is described in these standards. However, following the planning, execution and evidence gathering phases, there may be additional and specific issues that may lead to legal proceedings and to a final formal judgment on the matters of non-compliance. Such issues are not covered by this ISSAI 4000.

4

THE OBJECTIVE OF A COMPLIANCE AUDIT

- 23) The main objective of compliance auditing is to provide the intended user(s) with information on whether the audited public entities follow parliamentary decisions, laws, legislative acts, policy, established codes and agreed upon terms. These form the relevant authorities governing the subject matter/entity that is going to be audited. The authorities are the sources of audit criteria. The characteristics of the audit criteria are described in paragraph 118.
- 24) Compliance auditing includes both the aspects of regularity (adherence to formal criteria such as relevant laws, regulations and agreements) and/or propriety (observance of the general principles governing sound financial management and the conduct of public officials). Regardless of the source of criteria, the auditor performs the audit and forms a conclusion with the selected level of assurance, in accordance with the requirements in ISSAI 4000.
- 25) The audit criteria might already be defined by the national legislation and/or the remit of the audited entity. In these cases, a SAI will not always have ability to influence the scope of the audit work.
- 26) The SAI promotes good governance by identifying and reporting deviations from criteria, so that corrective action may be taken and so that those responsible are held accountable for their actions. Compliance audits are carried out by assessing whether activities, financial transactions and information comply, in all material respects, with the authorities that govern the audited entity. Fraud is an intentional act of misrepresentation and is an element which counteracts transparency, accountability and good stewardship.

- 27) Compliance auditing is generally conducted either:
 - a) As a separate compliance audit, or
 - b) In relation with the audit of financial statements, or
 - c) In combination with performance auditing.
- 28) The ISSAI 4000 does not provide detailed explanations on how to do combined audits.
- 29) An audit report provides important information as a base for decision making in the public sector. Audits provide this information based on sufficient and appropriate audit evidence. For each audit the needs of the intended user(s) are considered when deciding the level of assurance and hereby the level of sufficient and appropriate evidence. The auditor designs the audit to provide either a reasonable or a limited level of assurance.

CHARACTERISTICS OF AN ASSURANCE ENGAGEMENT

- 30) Every compliance audit is an assurance engagement. The auditor chooses the level of assurance based on the needs of the intended user(s). The audit report provides either reasonable or limited assurance.
- 31) Each assurance engagement is either an attestation engagement or a direct reporting engagement. Direct reporting engagement and attestation engagement differs based on who prepares and measure/evaluate the subject matter. The subject matter could either be set out in the mandate or selected by the SAI.
- 32) Regardless of the characteristics of the engagement, the audit criteria can

include both regularity and propriety.

REASONABLE ASSURANCE

- 33) 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.⁶
- 34) Normally a reasonable assurance would require more audit evidence than a limited assurance, which often means more extended audit procedures, for example, in matters of risk assessments, a better understanding of the entity environment, the evaluation of the design of the internal control system etc.

LIMITED ASSURANCE

- 35) 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. However, if the auditor believes that the subject matter is not in compliance with the criteria, s/he has to perform limited procedures to conclude whether the subject matter is in compliance with the criteria or not.
- 36) 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 user(s). A limited assurance report conveys the limited nature of the assurance provided.⁷

6 ISSAI 100/33.

7 ISSAI 100/33.

DIRECT REPORTING ENGAGEMENT

- 37) In a direct reporting engagement, it is the auditor who measures or evaluates the subject matter evidence against the criteria. The auditor is responsible for producing the subject matter information. The auditor selects the subject matter and criteria, taking into consideration risk and materiality. By measuring the subject matter evidence against the criteria, the auditor is able to form a conclusion. The conclusion is expressed in the form of findings, answers to specific audit questions, recommendations or an opinion.⁸
- 38) In a direct reporting engagement performed with reasonable assurance, the audit conclusion expresses the auditor's view that the subject matter is or is not compliant in all material respects with the applicable criteria.
- 39) When providing limited assurance, the conclusion conveys that nothing has come to the auditor's attention that the findings are not in compliance with the audit criteria. When the auditor has been aware of instances of non-compliance, the conclusion needs to reflect this.

ATTESTATION ENGAGEMENT

- 40) In an attestation engagement 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 forming a conclusion. The conclusion is expressed in the form of findings, conclusions, recommendations or an opinion.⁹
- 41) In an attestation engagement with reasonable assurance the auditor's conclusion expresses the auditor's view that the subject matter information is/is not in accordance with the applicable criteria.

8 ISSAI 100/29.

9 ISSAI 100/29.

- 42) In an attestation engagement with limited assurance the auditor states whether or not, based on the procedures performed, anything has come to her/his attention to cause the auditor to believe that the subject matter is not in compliance, in all material respects, with the applicable criteria. The procedures performed are limited compared with what is necessary to obtain reasonable assurance.

IDENTIFICATION OF SUBJECT MATTER AND SCOPE

- 43) Some SAIs have mandated requirements or have to perform audits on request from the Parliament, while other SAIs have discretion to select the coverage of compliance audits. The way in which the subject matter is selected, has an impact on the audit approach when it comes to audit evidence and resources.
- 44) The scope defines the subject matter, and what is going to be audited. The scope depends on the needs of the intended user(s), the decided level of assurance, the risk that has been assessed and the competence and resources available in the SAI.

5

GENERAL REQUIREMENTS OF COMPLIANCE AUDITING

OBJECTIVITY AND ETHICS

Requirement

- 45) The auditor shall comply with the relevant procedures relating to objectivity and ethics, which in turn shall comply with the related ISSAIs on objectivity and ethics.**

Explanation

- 46) The auditor is to demonstrate professional behaviour and integrity, be objective, possess the required professional competence, and exercise due care. S/he is also to maintain independence in fact and appearance and confidentiality regarding all audit matters.
- 47) The auditor can find additional guidance in *INTOSAI-P 10 - Mexico Declaration* on SAI Independence as well as *GUID 9030 - Good Practices Related to SAI Independence* and *ISSAI 130 Code of Ethics*.

Requirement

- 48) The auditor shall take care to remain objective so that findings and conclusions will be impartial and shall be seen as such by third parties.**

Explanation

- 49) The auditor demonstrates objectivity in selecting their audit objectives and identifying the criteria. The auditor needs to ensure that communication with stakeholders does not compromise the objectivity of the SAI.
- 50) The subject matter and audit criteria might already be defined by the national legislation and/or the remit of the audited entity. In these cases, a SAI will not always have ability to influence the scope of the audit work, but this restriction does not impact the objectivity of the auditor.
- 51) The auditor needs to avoid undue influence from any stakeholders in formulating a balanced report, and maintains their objectivity so that their work and report will be seen as impartial by reasonable and informed third parties.

AUDIT RISK

Requirement

- 52) The auditor shall perform procedures to reduce the risk of producing incorrect conclusions to an acceptable low level.**

Explanation

- 53) Reducing audit risk includes the following aspects: anticipating the possible or known risks of the work envisaged and consequences thereof, developing procedures to address those risks during the audit and documenting which and how those risks will be addressed. The auditor needs to evaluate whether the scope of the work performed is sufficient. In addition, when concluding, the auditor needs to evaluate whether s/he has sufficient and appropriate audit evidence when assessing subject matter against criteria to form conclusion(s), based on the level of risk involved.

- 54) In an attestation engagement the audit risk has three components:
- a) the subject matter's inherent risk (IR)
 - b) the control risk (CR); the risk that the relevant internal controls associated with the inherent risks are inappropriate or do not work properly
 - c) the detection risk (DR); the risk that the procedures performed by the auditor will lead to an incorrect conclusion/opinion

The three audit risk components (IR, CR and DR) are considered altogether during the evaluation of the audit risk.

- 55) In a direct reporting engagement, the auditor is involved in producing the subject matter information. The auditor may apply the audit risk model in forming a conclusion on the subject matter.
- 56) By identifying and evaluating the entity's inherent and control risks, the auditor can define the nature and extent of the evidence gathering procedures required to test compliance with the criteria. The higher the level of risk, the greater the extents of audit work that will be required to lower detection risk sufficiently to achieve the acceptable level of audit risk.
- 57) In the context of SAIs with jurisdictional powers considerations of audit risk may include:
- a) Identifying who may be held responsible for non-compliance acts.
 - b) Identifying the time period for which public officials may be held liable, taking into consideration the applicable prescriptive period, in order to avoid the failure of action.
 - c) Determining whether these acts have caused loss or waste of public funds.

RISK OF FRAUD

Requirement

- 58) The auditor shall consider the risk of fraud throughout the audit process, and document the result of the assessment.**

Explanation

- 59) The auditor needs to identify and assess the risk of fraud and obtain sufficient and appropriate audit evidence regarding the assessed risks, through designing and implementing appropriate responses.
- 60) Due to the inherent limitations of an audit, there is an unavoidable risk that unlawful acts, including fraud may occur and not be detected by the auditor. The risk of not detecting an unlawful act resulting from fraud is higher than the risk of not detecting one resulting from error. This is because fraud may involve organized schemes designed to conceal it, deliberate failure to record transactions, or intentional misrepresentations being made to the auditor. Such attempts at concealment may be even more difficult to detect when accompanied by collusion.
- 61) The auditor is responsible for maintaining professional scepticism throughout the audit and recognizing the fact that audit procedures that are effective for detecting error may not be effective in detecting fraud.
- 62) When suspected fraud has been identified, the auditor takes action to ensure that they respond appropriately according to the SAIs mandate and the particular circumstances.
- 63) The primary responsibility for the prevention and detection of fraud lies with the entity's management through designing, implementing and maintaining an adequate internal control system. Although an audit may act as fraud prevention, it is normally not designed to detect fraud.

SELECTION OF AREAS SIGNIFICANT FOR THE INTENDED USER(S)

Requirement

- 64) Where the SAI has discretion to select the coverage of compliance audits it shall identify areas that are of significance for the intended user(s).**

Explanation

- 65) Some SAIs have mandated requirements for compliance audits (Ref: Para. 25). For those SAIs, this requirement is not relevant.
- 66) When assessing the areas significant for the intended user(s) as a compliance audit, the SAI decides if the audit is going to be conducted as an attestation engagement or a direct reporting engagement.
- 67) Where the SAI has discretion to select the coverage of compliance audits, it performs the procedures necessary to identify significant areas and/or areas with potential risk of non-compliance. In performing these procedures, the auditor may take into consideration any of the following:
- a) Public or legislative interests or expectations.
 - b) Impact on citizens.
 - c) Projects with significant public funding.
 - d) Beneficiaries of public funds.
 - e) Significance of certain provisions of the law.
 - f) Principles of good governance.
 - g) Roles of different public sector bodies.
 - h) Rights of citizens and of public sector bodies.
 - i) Potential breaches of applicable laws and other regulations which govern the public entity's activity, or the public debt, public deficit and external obligations.

- j) Non-compliance with internal controls, or the absence of an adequate internal control system.
 - k) Findings identified in previous audits.
 - l) Risks of non-compliance signalled by third parties.
- 68) When performing these procedures, the auditor may find it valuable to read budget proposals, publications, evaluation reports etc. Taking part in conferences and discussion fora may also give the auditor valuable information to form the basis for selecting subject matters by the SAI and reduce the risk of auditing low risk areas.
- 69) The auditor may often come across examples of non-compliance in connection with other types of audit work being performed. It can be important to report the findings to the risk assessing process work in the SAI for the coming year.
- 70) After selecting the significant audit areas, the auditor needs to determine materiality (Ref: Para. 125).

PROFESSIONAL JUDGMENT AND SCEPTICISM

Requirement

- 71) The auditor shall exercise professional judgment throughout the audit process.**

Explanation

- 72) The exercise of professional judgment is crucial throughout the audit process. To exhibit professional judgment, the auditor attends relevant training, uses knowledge and experience within the context provided by auditing and ethical standards, so that well considered decisions can be made at all stages of the audit process.
- 73) The auditor uses professional judgment when deciding the level of assurance. The professional judgment is used when assessing risk and materiality,

defining the subject matter, scope and the corresponding audit criteria. Professional judgment is also used to assess procedures necessary to gather sufficient and appropriate audit evidence and the evaluation thereof. The use of professional judgment is crucial when analyzing the audit evidence and forming conclusions based on the findings.

Requirement

74) If expertise in a difficult or contentious issue is not available in the audit team, professional advice shall be sought.

Explanation

75) Difficult issues may require competence and experience not covered by the audit team. This can be issues related to business specific competence, juridical or methodological competence.

76) It is important to clarify contentious issues within the audit team, as well as between the audit team and any others involved in the audit.

Requirement

77) The auditor shall exercise professional scepticism, and maintain an open and objective mind.

Explanation

78) Professional scepticism is an attitude that includes maintaining an open and objective mind by being alert to conditions which may indicate possible non-compliance due to error or fraud. Professional scepticism is important when evaluating audit evidence contradicting other audit evidence already obtained, and information that brings into question the reliability of audit evidence, such as documents and responses to inquiries.

79) Exercising professional scepticism is necessary to ensure that the auditor avoids personal bias and to make sure that the auditor is not overgeneralizing when drawing conclusions from observations. In addition, the auditor will act rational based on a critical assessment of all the evidence collected.

QUALITY CONTROL

Requirement

- 80) The SAI shall take responsibility for the overall quality of the audit to ensure that the audits are carried out in accordance with relevant professional standards, laws and regulations, and that the reports are appropriate in the circumstances.**

Explanation

- 81) Within the scope of the quality control procedures, the SAI may have a quality assurance system in place to secure the overall quality of the audit.
- 82) The quality control procedures can be supervision, reviews, consultation and adequate training and might cover the planning, execution and reporting stage.
- 83) The overall quality of the SAI is dependent on a system where roles and responsibilities are clearly defined.
- 84) The SAI ensures that appropriate procedures are performed and that reviews are performed throughout the audit process. The quality controls are documented in the audit file.

Requirement

- 85) The SAI shall ensure that the audit team collectively has the necessary professional competence to perform the audit.**

Explanation

- 86) Quality control includes considering whether the audit team has sufficient and appropriate competence to conduct the audit, is capable of selecting criteria free from bias, has general access to accurate information, has considered available information, and has had sufficient time to complete the audit assignment.

- 87) The audit team is assembled to collectively have the necessary competence, knowledge, skills and expertise to perform the audit in accordance with professional standards.

Depending on the subject matter, this may include:

- a) Auditing skills and skills regarding data collection/analysis.
 - b) Legal competence.
 - c) An understanding and practical experience of the type of audit being undertaken.
 - d) Knowledge of the applicable standards and authorities.
 - e) An understanding of the audited entity's operations and appropriate experience for the type of entity and operations being audited.
 - f) The ability and experience to exercise professional judgment.
 - g) Producing an auditor's report that is appropriate in the circumstances.
- 88) The SAI needs to assign adequately skilled resources that are available when needed in the different phases of the audit process. Where specialized techniques, methods or skills are not available within the team or the SAI, external experts may be used in different ways, e.g. to provide knowledge or conduct specific work. When in need of external expertise, the SAI evaluates whether experts have the necessary independence, competence, capabilities and objectivity. The SAI also determines whether their work is adequate for the purposes of the audit. Even if external experts perform audit work on behalf of the SAI, the SAI is still responsible for the conclusion(s).

DOCUMENTATION

Requirement

- 89) The auditor shall prepare audit documentation that is sufficiently detailed to provide a clear understanding of the work performed, evidence obtained and conclusions reached. The auditor shall prepare the audit documentation in a timely manner, keep it up to date throughout the audit, and complete the documentation of the evidence supporting the audit findings before the audit report is issued.**

Explanation

- 90) The purpose of documenting the audit work performed is both to enhance transparency about the work performed, and to enable an experienced auditor having no previous connection with the audit, to understand significant matters arising during the audit, the conclusion(s)/ opinion(s) reached thereon, and significant professional judgments made in reaching those conclusion(s)/ opinion(s). The documentation includes as appropriate:
- a) An explanation of the subject matter of the audit.
 - b) Risk assessment, audit strategy and plan, and related documents.
 - c) The methods applied and the scope and time period covered by the audit.
 - d) The nature, the time and extent of the audit procedures performed.
 - e) The results of the audit procedures performed, and the audit evidence obtained.
 - f) The evaluation of the audit evidence forming the finding(s), conclusion(s) opinion(s) and recommendation(s).
 - g) Judgments done in the audit process, including professional consultations and the reasoning behind them.
 - h) Communication with and feedback from the audited entity.
 - i) Supervisory reviews and other quality control safeguards undertaken.

- 91) Documentation needs to be sufficient to demonstrate how the auditor defined the audit objective, subject matter, the criteria and the scope¹⁰, as well as the reasons why a specific method of analysis was chosen. For this purpose, documentation needs to be organized in order to provide a clear and direct link between the findings and the evidence that support them.
- 92) Specifically related to the audit planning stage, the documentation kept by the auditor needs to contain:
- a) The information needed to understand the entity being audited and its environment which enable the assessment of the risk.
 - b) The assessment of the materiality of the subject matter.
 - c) The identification of possible sources of evidence.
- 93) The auditor needs to adopt appropriate procedures to maintain the confidentiality and safe custody of the audit documentation, and retain it for a period sufficient to meet the needs of the legal, regulatory, administrative and professional requirements of record retention and to enable the conduct of audit follow-up activities.
- 94) Documenting the key decisions made is important to demonstrate the independence and impartiality of the auditor in his/her analysis. The existence of sensitive issues demands the documentation of the relevant facts considered by the auditor in choosing a particular course of action or in taking a certain decision. In this way, the actions and decisions are explained and transparent.
- 95) In the context of SAIs with jurisdictional powers, documentation needed to provide proposals of personal liability is outside the scope of this professional standard.

10 The scope needs to narrow things to enable the auditor to conduct proper audits.

COMMUNICATION

Requirement

- 96) The auditor shall communicate in an effective manner with the audited entity and those charged with governance throughout the audit process.**

Explanation

- 97) The matters that are communicated in writing to the audited entity may include: the audit subject matter, audit criteria, the level of assurance, the time period for the audit, and the government undertakings, organizations and/or programs to be included in the audit, i.e. confirming the terms of engagement. Communicating these matters can help in achieving mutual understanding of the audit process and the auditees operations.
- 98) The form of communication with those charged with governance throughout the audit process needs to be adapted to the conditions. The auditor considers the timing of communications, and whether they are conducted orally or in writing or both.

Requirement

- 99) Instances of material non-compliance shall be communicated with the appropriate level of management and (if applicable) those charged with governance. Other significant matters arising from the audit that are directly relevant to the entity shall also be communicated.**

Explanation

- 100) Findings that are not deemed material, or do not warrant inclusions in the auditor's report, may also be communicated to management during the audit. Communicating such findings may help the audited entity to remedy instances of non-compliance and avoid similar instances in the future.

6

REQUIREMENTS RELATED TO THE COMPLIANCE AUDITING PLANNING PROCESS

IDENTIFYING INTENDED USER(S) AND RESPONSIBLE PARTY

Requirement

101) The auditor shall explicitly identify the intended user(s) and the responsible party and consider the implication of their roles in order to conduct the audit and communicate accordingly.

Explanation

- 102) The intended user(s) are the persons for whom the auditor prepares the compliance audit report. The intended user(s) may be legislative or oversight bodies, those charged with governance the public prosecutor, media or the general public. The responsible party is responsible for the subject matter, and is as such the subject for the audit.
- 103) When planning the audit, the auditor chooses the materiality, based on the needs of the intended user(s).
- 104) Identification of the responsible party is important when setting the audit criteria. The responsible party needs to comply with criteria deriving e.g. from laws, regulations, budgetary laws and financial regulations. Depending on the subject matter, the auditor chooses the relevant audit criteria. The auditor also needs to communicate with the responsible party on several occasions throughout the audit process.

- 105) In determining the level of assurance to be provided and how this assurance should be communicated, the auditor needs to identify the intended user(s) and their needs.
- 106) For some subject matters it can be relevant to include more than one responsible party. This could be the case e.g. when more than one entity is involved in the execution of the budget. In those cases, the number of intended user(s) may also increase.

DEFINING THE SUBJECT MATTER AND THE CORRESPONDING AUDIT CRITERIA

Requirement

- 107) Where the SAI has discretion to select the coverage of compliance audits, the auditor shall define the subject matter to be measured or evaluated against criteria.**

Explanation

- 108) Based on identified audit areas (Ref: Para. 67), the auditor defines the subject matter of the audit.
- 109) The subject matter should be identifiable, and possible to assess against suitable audit criteria. It should be of such nature that it enables the auditor to conclude with the necessary level of assurance. This means to gather sufficient and appropriate audit evidence to support the audit conclusion or opinion.

Requirement

- 110) Where the SAI has discretion to select the coverage of compliance audits, the auditor shall identify relevant audit criteria prior to the audit to provide a basis for a conclusion/an opinion on the subject matter.**

Explanation

- 111) The subject matter and audit criteria are linked and consistent. Therefore, identifying the corresponding audit criteria is an iterative process.
- 112) When auditing a subject matter, the auditor has to make sure that there are corresponding audit criteria.
- 113) The subject matter and relevant audit criteria might already be defined by the mandate of the SAI or national legislation.¹¹ In an attestation engagement the audit criteria are implicitly given by the presentation of the subject matter information. In these cases, the auditor needs to identify relevant audit criteria to draw conclusions on correctness of criteria implicitly given in the subject matter information by the responsible party.
- 114) Legal criteria can derive from:
- a) Rules and regulations.
 - b) International treaties and other agreements.
 - c) Codes of conduct.
- 115) A compliance audit may be concerned with regularity or with propriety (observance of the general principles governing sound financial management and the conduct of public officials). While regularity is the main focus of compliance, propriety may also be pertinent given the public-sector context, in which there are certain expectations concerning financial management and the conduct of public officials. Depending on the mandate of the SAI, audits may also examine compliance with generally accepted principles and generally acknowledged best practice governing the conduct of public officials

11 Relevant audit criteria derive from the primary legislation defined as legislation enacted by law making authorities/bodies like parliament etc. Subordinate legislation may be defined as legislation enacted by authorities/bodies delegated to enact them under the primary legislation. Audit criteria also derive from Constitution, the international treaties, including among others, the treaties creating international or supranational organizations, the treaties with binding fiscal or budgetary content, legal ruling issued by the competent institutions of international or supranational organizations with direct and binding effect in the legal order of each member State, laws and regulations issued by the competent institutions of each State, in compliance with their Constitution, including the constitutional budgetary laws, the annual budgetary laws, other laws, regulations with financial effect in the public management, public governance, public procurement conflict of interests, safeguard of public monies and public assets prevention and detection of fraud and corruption and relevant accounting principles. They may also comprise authoritative decisions taken by international, supranational or national courts, as deriving from the Constitution and the international treaties that empower those courts. Finally, they may also comprise statutory instruments, rules, regulations, qualities and orders, governmental or ministerial directives, guidelines and agreed upon terms and conditions.

(propriety).¹² Suitable audit criteria for a compliance audit of propriety will be either generally-accepted principles or national or international best practice. In some cases they may be uncodified, implicit or based on overriding principles of law.¹³ This would provide sufficient flexibility to the Supreme Audit Institutions to adopt criteria relevant to their country in audit against propriety.

116) Suitable propriety criteria may derive from:

- a) Public financial management expectations such as compliance with effective and efficient internal control system.
- b) Beneficiaries' expectations regarding the utility of goods, or the quality of the services and works.
- c) Requirements for a transparent and unbiased allocation of public funds and human resources.

117) In some cases, laws and regulations require further interpretation in order to derive relevant audit criteria. If situations arise where there are conflicting provisions or there may be doubt as to what is the correct interpretation of the relevant law, regulation or other authorities, the auditor may find it useful to consider the intentions and premises set out in developing the law, or to consult with the particular body responsible for the legislation. The auditor may also consider relevant earlier decisions made by judicial authorities.

118) Suitable audit criteria either regularity or propriety, exhibit the following characteristics:

- I) **Relevance:** Relevant criteria result in subject matter information that assists decision-making by the intended user(s).
- II) **Completeness:** Criteria are complete when subject matter information prepared in accordance with them does not omit relevant factors that could reasonably be expected to affect decisions of the intended user(s) made on the basis of that subject matter information.
- III) **Reliability:** Reliable criteria result in consistent conclusions when used and examined in the same way, by another auditor, in the same circumstances.

¹² ISSAI 400/13.

¹³ ISSAI 400/32.

- IV) **Neutrality:** Neutral criteria result in subject matter information that is free from bias as appropriate in the engagement circumstances.
 - V) **Understandability:** Understandable criteria result in subject matter information that can be understood by the intended user(s).
 - VI) **Usefulness:** Useful criteria result in findings and conclusions that meet user(s)' information needs.
 - VII) **Comparability:** Comparable criteria are consistent with those used in Compliance Audits of other similar agencies or activities and with those used in previous Compliance Audits of the entity being audited.
 - VIII) **Acceptability:** Acceptable criteria are those that independent experts in the field, audited entities, legislature, media, and general public generally agree to.
 - IX) **Availability:** The criteria are available for intended user(s) in such way that they understand the nature of the audit work performed and the basis for the audit report.
- 119) Once suitable criteria have been identified based on the characteristics set out above, they then must be appropriately operationalized for the particular circumstances of each audit so as to be able to reach meaningful conclusion(s).
- 120) If, while executing the audit, the auditor identifies breaches of other suitable audit criteria than those criteria identified in the planning phase, the auditor has a responsibility to report these breaches.

DETERMINING THE LEVEL OF ASSURANCE

Requirement

- 121) Depending on the mandate of the SAI, the characteristics of the subject matter, and the needs of the intended user(s), the auditor shall decide whether the audit shall provide reasonable or limited assurance.**

Explanation

- 122) When assessing the level of assurance, the auditor considers the needs of the intended user(s). This could be done through communicating with the intended user(s) or those charged with governance. There may also be generally accepted practices in the jurisdiction to support the auditor in deciding the level of assurance.
- 123) Providing reasonable assurance requires more extensive audit work (Ref: Para. 34).
- 124) Some SAIs have mandated requirements which already define the level of assurance.

DETERMINING MATERIALITY

Requirement

- 125) The auditor shall determine materiality to form a basis for the design of the audit, and re-assess it throughout the audit process.**

Explanation

- 126) Materiality reflects the assessed needs of the intended user(s), (Ref: Para 64), and these needs have to be identified when planning the audit. Based on the selected subject matter, materiality is determined by identifying the level of non-compliance that is likely to influence the decisions of the intended user(s). In identifying materiality, the auditor pays attention to specific areas of legislative focus, public interest or expectations, requests and significant public funding as well as fraud.¹⁴
- 127) The concept materiality includes nature, context and value. Materiality may focus on quantitative factors such as the number of persons or entities affected by the particular subject matter or the monetary amounts involved as well as the misuse of public funds, regardless of the amount. Materiality is often considered in terms of value, but the inherent nature or characteristics of an item or group of items may also render a matter material (qualitative factors).

¹⁴ ISSAI 400/47.

- 128) Materiality is applied by the auditor in planning and executing the audit, and in evaluating the effect of instances of non-compliance. In the planning phase, assessing materiality helps the auditor to identify the audit questions which are of importance to the intended user(s). In performing the audit, the auditor uses materiality in the decision of the extent of audit procedures to be executed and the evaluation of audit evidence. In evaluating and concluding the audit, the auditor uses materiality to evaluate the scope of work and the level of non-compliance to determine the impact on the conclusion/opinion.
- 129) Quantitative materiality is determined by applying a percentage to a chosen benchmark as a starting point (Ref: Para. 186). This involves the exercise of professional judgment and reflects, in the auditor's judgment, the measures that user(s) of the information are most likely to consider important. Quantitative materiality is mostly used in attestation engagement. When performing such engagements, the auditor might want to select separate levels of materiality for classes of transactions or balances that are more important to the user(s) of the accounts or have a higher risk of non-compliance material by nature or context.
- 130) In some cases, the qualitative factors are more important than the quantitative factors. Public expectations and public interest are examples of qualitative factors that may impact the auditor's determination of materiality. Instances of excess spending over appropriations authorized by the legislature or introduction of a new service not provided for in the approved appropriations, may be instances of non-compliance that are not material but may still warrant communication to the auditee due to their nature.

UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT INCLUDING THE INTERNAL CONTROL

Requirement

131) The auditor shall have an understanding of the audited entity and its environment, including the entity's internal control, to enable effective planning and execution of audit.

Explanation

132) The auditor needs to understand the entity and its environment and how this may influence the subject matter and the subject matter information.

133) To obtain an understanding of the entity and its environment, the auditor may consider the relevant business, laws and regulations, other external factors, the nature of the entity's operations, governance arrangements, objectives and strategies or performance measures. This understanding may be documented in the audit strategy.

134) The auditor needs to obtain an understanding of the entity's internal control relevant to the audit. When the subject matter is determined, the auditor identifies the internal controls that are in place to reduce the risk of non-compliance with criteria or material misstatements in the subject matter information. By using professional judgment, the auditor decides whether a control is relevant to the audit or not.

135) An internal control system is composed of policies, structures, procedures, processes and tasks that help the audited entity to respond appropriately to risks of non-compliance with the criteria. An effective system may safeguard the audited entity's assets, facilitate internal and external reporting and help the audited entity to comply with relevant authorities. The auditor needs to obtain an understanding of all components of an internal control system: the control environment, the entity's risk assessment process, the information system, the control activities relevant to the audit and the monitoring of control relevant to the audit.

- 136) To obtain an understanding of the internal control, 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, organizational structure, the existence and level of internal audit activity, the assignment of authority and responsibility, and human resource policies and practices.

AUDIT STRATEGY AND AUDIT PLAN

Requirement

- 137) The auditor shall develop and document an audit strategy and an audit plan that together describe how the audit will be performed to issue reports that will be appropriate in the circumstances, the resources needed to do so and the time schedule for the audit work.**

Explanation

- 138) The audit strategy is the basis for deciding whether the audit is possible to execute. The audit strategy describes what to do, and the audit plan how to do it.
- 139) The purpose of the audit strategy is to document/design the overall decisions, and may contain the following:
- a) The audit objective, subject matter, scope, criteria and other characteristics of the compliance audit taking into account the mandate of the SAI.
 - b) The type of engagement (attestation engagement or direct reporting engagement).
 - c) The level of assurance to be provided.
 - d) Composition and work allocation of the audit team, including any need for experts, and the dates of quality control.
 - e) Communication with the auditee and/or those charged with governance.

- f) Reporting responsibilities, as well as to whom and when such reporting will take place, and in what form.
 - g) The entities covered by the audit.
 - h) The materiality assessment.
- 140) The auditor develops an audit plan for the compliance audit. The audit strategy is an essential input to the audit plan. The audit plan may include:
- a) Nature, timing and extent of planned audit procedures and when they will be performed.
 - b) An assessment of risk and of internal controls relevant for the audit.
 - c) The audit procedures designed as a response to risk.
 - d) The potential audit evidence to be collected during the audit.
- 141) The auditor updates both the audit strategy and the audit plan as necessary throughout the audit.
- 142) When planning and performing compliance audits, the auditor operating in SAIs with jurisdictional powers may take into consideration the need to:
- a) Identify the person(s) who may be held liable for acts of non-compliance.
 - b) Take into consideration any applicable prescription period.
 - c) Distinguish personal liability for acts of non-compliance from the liability for unlawful acts (suspected fraud).
- 143) In some jurisdictions, compliance audits might be undertaken as an integral part of the audit of financial statements. The auditor might find it efficient to embed an audit strategy, an audit plan and audit procedures required for compliance audit into those required for the audit of financial statements.

7

REQUIREMENTS RELATED TO PERFORMING AUDIT PROCEDURES TO OBTAIN AUDIT EVIDENCE

SUFFICIENT AND APPROPRIATE AUDIT EVIDENCE

Requirement

- 144) The auditor shall plan and perform procedures to obtain sufficient and appropriate audit evidence to form a conclusion with the selected level of assurance.**

Explanation

- 145) The nature and sources of the necessary audit evidence shall be determined by the desired level of assurance, the criteria, materiality, the subject matter and the scope of the audit.
- 146) Sufficient audit evidence is related to the decision about the level of assurance. To form a conclusion with reasonable assurance, the auditor needs to obtain more evidence than in a limited assurance engagement. The nature of audit evidence is also different for the two types of audits. For limited assurance engagements the audit evidence is mostly analytical procedures and inspections while for reasonable assurance engagements the auditor normally needs to perform mostly all the audit techniques (Ref: Para. 160).
- 147) Sufficiency is a measure of the quantity of evidence needed to support the audit findings and conclusions. In assessing the sufficiency of evidence, the auditor needs to determine whether enough evidence has been obtained to persuade a knowledgeable person that the findings are reasonable.

- 148) Appropriateness is a measure of the quality of the evidence, it encompasses relevance, validity and reliability. Relevance refers to the extent to which the evidence has a logical relationship with, and importance to, the issue being addressed. Validity refers to the extent to which the evidence is a meaningful or reasonable basis for measuring what is being evaluated. In other words, validity refers to the extent to which the evidence represents what it is purported to represent. Reliability refers to the extent to which the audit evidence has been gathered and produced with a transparent and reproducible method.
- 149) The auditor needs to plan appropriate responses to assessed risks. Responses to assessed risks include designing audit procedures that address the risks, such as substantive procedures and tests of controls. Substantive procedures include both tests of details and analytical procedures. If the auditor intends to rely on the operating effectiveness of control s/he needs to obtain evidence that the controls are operating effectively when determining the nature, timing and extent of substantive procedures. The design and implementation of key controls relevant to the subject matter might be evaluated as adequate.
- 150) The evidence gathering process continues until the auditor is confident that sufficient and appropriate evidence exists to support the agreed level of assurance to support the auditor's conclusion or opinion.
- 151) The quantity of evidence required depends on the audit risk (the greater the risk, the more evidence is likely to be required) and on the quality of such evidence (the higher the quality, less evidence may be required). But at the same time the auditor always assesses that the amount of evidence depends on the specifics of a particular audit, and not only on the quantity or quality of audit evidence. Accordingly, the sufficiency and appropriateness of evidence are interrelated.
- 152) Merely obtaining more evidence does not compensate for its poor quality. The reliability of evidence is influenced by its source and nature, and is dependent on the specific circumstances in which it was obtained. The auditor considers both the relevance and the reliability of the information to be used as audit evidence.

Requirement

153) The auditor in a SAI with jurisdictional powers shall perform procedures to obtain sufficient and appropriate audit evidence regarding the liability of the public official who might be held responsible for non-compliance/unlawful acts.

Explanation

154) In planning and performing audits, the auditor in SAIs with jurisdictional powers needs to gather sufficient and appropriate evidence regarding the liability of the public official who might be held responsible for non-compliance/unlawful acts.

155) The evidence gathering process continues until the auditor in SAIs with jurisdictional powers is satisfied that sufficient and appropriate evidence exists to provide a basis for the auditor's conclusion on whether persons responsible for the non-compliance are liable for any loss, misuse or waste of public funds and ought to be discharged for their mismanagement.

156) The auditor in SAIs with jurisdictional powers evaluates, based on his/her professional judgment, whether there is sufficient and appropriate evidence that the public official can be held personally liable for acts of non-compliance.

157) Professional judgment in determining whether or not the public official is personally liable for non-compliance acts may include:

- a) An assessment of the way the responsibilities mentioned by the law or included in the public official's job description were carried out.
- b) Determining whether the public official's non-compliance or unlawful act caused the identified loss, misuse or waste of public funds or goods.
- c) An assessment of the possible liability exemption circumstances (i.e. force majeure, unforeseeable circumstances).
- d) An assessment of the relationships between public accountants and public managers, and the possible effects and consequences non-compliance acts may have.

Requirement

158) The auditor shall select a combination of audit techniques to be able to form a conclusion with the selected level of assurance.

Explanation

159) The auditor performs effective audit procedures in line with the audit plan to gather audit evidence and fulfil audit objectives. The auditor will often need to combine and compare evidence from sources using different techniques/methods in order to meet the requirements for sufficiency and appropriateness. For example, by interviewing management and employees, the auditor may obtain an understanding of how management shares its views on the entity's practices and ethical behaviour with staff. 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 is followed in practice. A survey submitted to the employees could for example illuminate to what extent the management acts in accordance with the code of conduct. Based on the scope, the auditor will gather quantitative or qualitative audit evidence, or a combination thereof.

160) Audit evidence is gathered using a variety of methods such as:

- a) Observation
- b) Inspection
- c) Inquiry
- d) External confirmation
- e) Re-performance
- f) Re-calculation
- g) Substantive testing
- h) Test of key controls
- i) Analytical procedures

- 161) Observation involves looking at a process or procedure being performed by others. Observation provides audit evidence of the performance of a process or procedure, but is limited to the point in time at which the observation takes place, and by the fact that the act of being observed may affect how the process or procedure is performed.
- 162) Inspection involves examining books, records or documents, whether internal or external, either in paper form, electronic form or a physical examination. The auditor considers the reliability of any documents inspected and remains conscious of the risk of fraud and the possibility that documents inspected may not be authentic.
- 163) Inquiry involves seeking information from relevant persons, both within and outside the audited entity. Depending on the subject matter and the scope, only interviews and questionnaires will in most cases not be sufficient and appropriate evidence. Other relevant evidence gathering methods to be considered are e.g. written documentation from the audited entity.
- 164) External confirmation represents audit evidence obtained by the auditor as a direct written response to the auditor from a third party. Hence, the auditor is obtaining feedback directly from beneficiaries or third parties that are not beneficiaries that they have received the grants or other funds that the audited entity asserts have been paid out, or confirming that funds have been used for the particular purpose set out in the terms of a grant or funding agreement.
- 165) Re-performance involves independently carrying out the same procedures already performed by the audited entity, controls that were originally performed as part of the entity's internal control. Re-performance may be done manually or by computer assisted audit techniques. Where highly technical matters are involved, external experts may be involved.
- 166) Re-calculation consists of checking the mathematical accuracy of documents or records. Re-calculation may be performed manually or electronically.
- 167) Substantive testing involves testing detailed transactions or activities against the audit criteria. Substantive testing is mostly used in attestation engagements and must always be included as an audit technique in such engagements. However, performing only substantive testing is only effective in rare cases and this audit technique will normally be combined with other audit techniques.

- 168) Test of key controls involves testing the controls that management has put in place to reduce the risk of non-compliance or the risk that the subject matter information is materially misstated. For most subject matters, testing key controls is an effective way to collect audit evidence.
- 169) Analytical procedures can be used both as part of the risk analysis and when collecting audit evidence. Audit evidence can be collected either by comparing data, investigating fluctuations or identifying relationships that appear inconsistent with what was expected, either based on historical data or the auditor's past experience. Regression analysis techniques or other mathematical methods may assist public sector auditors in comparing actual to expected results. Analytical procedures can never be the only technique used. In a limited assurance engagement, analytical procedures and inspections are normally enough to form a conclusion with limited assurance while a conclusion with reasonable assurance must be formed on the basis of a combination of the audit techniques mentioned in paragraph 158.

Requirement

- 170) In SAIs with jurisdictional powers, the inquiry shall be carried out in written form when requested by the national law.**

Explanation

- 171) SAIs with jurisdictional powers may, in particular, use the method of inquiry as set out in the laws governing the auditing procedures. This may involve preparing and sending a written communication to the relevant responsible persons asking for specific information which the audit team considers to be necessary to support the conclusion(s).

AUDIT SAMPLING

Requirement

- 172) The auditor shall use audit sampling, where appropriate, to provide a sufficient amount of items to draw conclusions about the population from**

which the sample is selected. When designing an audit sample, the auditor shall consider the purpose of the audit procedure and the characteristics of the population from which the sample will be drawn.

Explanation

- 173) Audit sampling is defined as the application of audit procedures to less than 100 percent of items within a population of audit relevance.
- 174) A sample may be quantitative or qualitative depending on the audit scope, and the need for information to illuminate the subject matter from several angles.
- 175) Quantitative sampling is used when the auditor seeks to draw conclusions about the whole population by testing a sample of items selected from it. In quantitative sampling, the sample risk must be reduced to an acceptable low level. However, the technical approach to quantitative sampling may require statistical techniques. If the audit team does not have the skills to apply them, a statistician expert may be required.
- 176) Qualitative sampling¹⁵ is a selective procedure conducted as a deliberate and systematic process to identifying the factors of variation in the subject matter. The auditor might sample on the basis of characteristics of individuals, groups, activities, processes or the audited entity as a whole. Qualitative sampling always requires careful assessment and sufficient knowledge of the subject matter.
- 177) When the auditor selects cases for in-depth study, it usually results in relatively small samples that can answer more explorative questions and provide new information, analyses and insight of the subject matter.
- 178) It may be appropriate to use risk-based sampling instead of a statistical approach when selecting items for testing, for instance when addressing a significant risk.

15 Examples of such techniques can be heterogeneous sampling (dissimilar), homogenous sampling (similar), critical-case sampling and deviant case sampling.

8

REQUIREMENTS RELATED TO EVALUATING AUDIT EVIDENCE AND FORMING CONCLUSIONS

Requirement

179) The auditor shall compare the obtained audit evidence with the stated audit criteria to form audit findings for the audit conclusion(s).

Explanation

180) The gathered evidence as well as the entities views is evaluated using professional judgment and scepticism.

181) In the evaluation process, the auditor assesses whether there is sufficient and appropriate audit evidence to form a conclusion.

182) For a balanced and objective view, the evaluation process entails considering all evidence provided in relation to the audit findings.

183) By evaluating the scope of work performed, the auditor determines whether s/he is able to draw a conclusion. If the scope of work is insufficient, the auditor might consider performing further procedures or modifying his/her opinion due to scope limitation.

Requirement

184) Based on the audit findings, and the materiality, the auditor shall draw a conclusion whether the subject matter is, in all material respects, in compliance with the applicable criteria.

Explanation

- 185) Based on the materiality, the auditor evaluates whether the audit findings are material enough to conclude that the subject matter in all material respect is not in compliance with the audit criteria. Depending on the characteristics of the subject matter, the auditor takes into consideration both value, nature and context. This means that instances of non-compliance that would be considered material by nature or context by the intended user(s), can also lead to a conclusion on non-compliance.
- 186) Materiality by value can involve amounts involved (monetary amounts) or other quantitative measures such as number of citizens or entities involved, carbon emission levels, time delays in relation to deadlines, etc. (Ref: Para.129).
- 187) The auditor may also include:
- a) Visibility and sensitivity of the program in question (for example, is it the subject of significant public interest, does it impact vulnerable citizens, etc.).
 - b) Needs and expectations of the legislature, the public or other users of the audit report.
 - c) The nature of the relevant authorities.

Requirement

188) The auditor shall communicate the level of assurance provided in a transparent way.

Explanation

- 189) The auditor needs to give the intended user(s) confidence in the audit results. This is done by explaining how findings, criteria and conclusions were developed in a balanced and reasoned manner and how certain overall conclusion(s) or recommendation(s) were reached based on the findings.
- 190) For direct reporting engagements, the auditor needs to implicitly state whether the conclusion is given with limited or reasonable assurance. For attestation engagement, the level of assurance will be conveyed by the appropriate use of standardised audit opinions.

9

REQUIREMENTS RELATED TO REPORTING

Requirement

191) The auditor shall communicate the conclusion in an audit report. The conclusion can be expressed either as an opinion, conclusion, answer to specific audit questions or recommendations.

Explanation

192) An opinion is a clear written statement of the auditor expressed in a standardized format, either unmodified or modified. It is stated in the audit report whether instances of non-compliance are pervasive. An opinion is normally used in an attestation engagement.

193) Where no material instances of non-compliance have been identified, the opinion is unmodified. An example of the form for an unmodified opinion for a reasonable assurance engagement (where appropriate wording is inserted in the brackets as applicable) may be as follows. "In our opinion [the audited entity's subject matter] is in compliance, in all material respects, with [the applied criteria]."

194) The auditor modifies his/her opinion in cases of:

a) Material instances of non-compliance. Depending on the extent of the non-compliance, this may result in:

l) A qualified opinion (if compliance deviations are material, but not pervasive): "Based on the audit work performed, we found that except for [describe exception], the audited entity's subject matter is in compliance, in all material respects with [the applied criteria]...", or

- II) An adverse opinion (if compliance deviations are material and pervasive): “In our opinion, [the subject matter] is not in compliance... in all material respect with (the applied criteria)...and compliance deviations are pervasive” or
- b) Scope limitation. Depending on the extent of the limitation, this may result in:
- III) A qualified opinion (if the auditor is unable to obtain sufficient and appropriate audit evidence, and the possible effects are material, but not pervasive): “In our opinion, except for [describe exception], the auditor were unable to obtain sufficient and appropriate audit evidence, and the possible effects are material, but not pervasive.”, or
- IV) A disclaimer (if the auditor is unable to obtain sufficient and appropriate audit evidence on compliance with authorities, and the possible effects are material and pervasive): “We do not express an opinion on the subject matter. We have not been able to obtain sufficient and appropriate audit evidence to provide a basis for an opinion...”.
- 195) In a limited assurance engagement an example of an unmodified opinion may be: “Based on the work performed described in this report, nothing has come to our attention that causes us to believe that the subject matter is not in compliance, in all material respects with the [applied criteria]”. A modified opinion can state that: “Based on the work performed described in this report, except for [describe exception] nothing has come to our attention that causes us to believe that the subject matter is not in compliance, in all material respects with the [applied criteria]”.
- 196) The wording of the opinion should reflect the mandate of the SAI. The auditor may therefore use terms such as “is legal and regular”, “is regular” or “has been applied to the purposes intended by the Parliament”.
- 197) In a reasonable assurance engagement with an unmodified opinion, the auditor states that the audit evidence obtained is sufficient and appropriate to provide a basis for the opinion.

- 198) In an attestation engagement, the auditor provides assurance by making a clear statement of the level of assurance, either through standardized opinions or conclusions.
- 199) In direct reporting, the auditor can provide assurance either by:
- a) making a clear statement of the level of assurance, through conclusions which explicitly convey the level of assurance, or
 - b) 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.¹⁶
- 200) In a reasonable assurance engagement, the auditor gathers sufficient and appropriate audit evidence to conclude whether the subject matter complies in all material respects with identified suitable criteria, and provides a report in the form of a positive assurance.
- 201) In a limited assurance engagement, the auditor gathers sufficient and appropriate evidence to address the engagement objective; however, the procedures are limited compared to what is necessary in a reasonable assurance engagement. The auditor then concludes, if appropriate, that 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.

Requirement

- 202) The auditor shall prepare an audit report based on the principles of completeness, objectivity, timeliness, accuracy and contradiction.**

Explanation

- 203) In an attestation engagement and a direct reporting engagement the conclusion should be sufficiently clear to remove the risk of misinterpretation.
- 204) Reporting is one of the essential parts of the audit. The forms of reporting may be defined in law or by the mandate of the SAI. A written report, setting

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out findings, opinions, conclusions, and recommendations in an appropriate form as applicable, is to be prepared at the end of each audit.

- 205) The principle of completeness requires the auditor to consider all relevant audit findings before issuing a report.
- 206) The principle of objectivity requires the auditor to apply professional judgment and scepticism in order to ensure that the report is factually correct and that findings and conclusions are presented in a relevant, fair and balanced manner.
- 207) The principle of timeliness implies preparing the report in due time to be relevant for the intended user(s).
- 208) The principle of accuracy and consultation implies checking the accuracy of facts with the audited entity.
- 209) The principle of contradiction implies incorporating responses from the responsible entity as appropriate and giving answers and assessments of the responses.

REPORT STRUCTURE - DIRECT REPORTING ENGAGEMENT

Requirement

- 210) The audit report shall include the following elements (although not necessarily in this order):**
- a) Title.
 - b) Identification of the auditing standards.
 - c) Executive summary (as appropriate).
 - d) Description of the subject matter and the scope (extent and limits of the audit).
 - e) Audit criteria.
 - f) Explanation and reasoning for the methods used.
 - g) Findings.

- h) Conclusion(s) based on answers to specific audit questions or opinion.
- i) Replies from the audited entity (as appropriate).
- j) Recommendations (as appropriate).

Explanation

- 211) The executive summary of the work performed and methods used helps the intended user(s) understand the auditor's conclusion. For many audits, broad variations in procedures are possible. In practice, however, these are difficult to communicate clearly and unambiguously. Hence, the executive summary of the work performed and methods used need to give a brief explanation for an outside reader of how the audit was performed.
- 212) The audit criteria section could state that in the audit report the laws, legislation, rules and regulations that were used in the audit should explicit be identified in the audit report.
- 213) The findings section comprises the auditor's comparison of the obtained evidence against the stated criteria and how this comparison has led to the audit findings.
- 214) Incorporating responses from the audited entity provides an indication of agreement to take action on the matter reported. Discussing the draft report findings with the audited entity helps ensure that these are complete, accurate and fairly presented.
- 215) Where significant compliance deviations are reported, recommendations are provided in cases where there is potential for significant improvement. It may be helpful to user(s) that the auditor highlights ongoing corrective actions.
- 216) While constructive and practical recommendations assist in promoting sound public sector management, the auditor is careful not to provide such detailed recommendations so as to be taking on the role of management and thereby risk impairing his or her own objectivity.
- 217) Recommendations might be issued separately from the report as they are usually written mainly for the management of the audited entity. In these instances, the recommendations might be issued separately in a letter to management.

REPORT STRUCTURE - ATTESTATION ENGAGEMENT

Requirement

218) The audit report shall include the following elements (although not necessarily in this order):

- a) Title.
- b) Addressee.
- c) Description of the subject matter information, and when appropriate the underlying subject matter.
- d) Extent and limits of the audit including the time period covered.
- e) Responsibilities of the responsible party and the auditor.
- f) Audit criteria.
- g) Identification of the auditing standards and level of assurance.
- h) A summary of the work performed and methods used.
- i) Opinion/conclusion.
- j) Replies from the audited entity (as appropriate).
- k) Report date.
- l) Signature.

Explanation

219) In some SAIs the results from the compliance audit is reported together with the audit on the financial statement. The SAI then makes sure that the requirements are covered either through separate compliance audit elements or as part of the financial audit elements.

220) Normally recommendations are not included in the attestation engagement reports. Recommendations might be issued separately in a letter to management.

ADDITIONAL REPORT STRUCTURE - SAIS WITH JURISDICTIONAL POWERS

Requirement

221) In the SAIs with jurisdictional powers, the auditor shall consider the role of the prosecutor or those responsible for dealing with judgment issues within the SAI, and shall also include as appropriate, the following elements in both direct reporting and attestation engagements:

- a) Identification of the responsible parties and the audited entity.
- b) The responsible person(s) involved and their responsibilities.
- c) Identification of the auditing standards applied in performing the work.
- d) Responsibilities of the auditor.
- e) A summary of the work performed.
- f) Operations and procedures etc. that are affected by non-compliance acts and/or possible unlawful acts. This needs to include, as appropriate:
 - A description of the finding and of its cause,
 - The legal act which has been infringed (the audit criteria),
 - The consequences of the non-compliance acts and/or possible unlawful acts.
- g) The responsible persons and their explanations regarding their non-compliance acts and /or possible unlawful acts, when appropriate.
- h) The auditor's professional judgment which determines whether there is personal liability for non-compliance acts.
- i) The value of the loss/misuse/waste created and the amount to be paid due to personal liability.

- j) Any measures taken by responsible persons during the audit to repair the loss/misuse/waste created.
- k) The management's arguments on the non-compliance/unlawful acts.

Explanation

- 222) In the case of audits conducted by SAIs with jurisdictional powers, the user(s) of compliance audit reports include the prosecutor or those responsible for dealing with judgment issues within the SAI.
- 223) SAIs with jurisdictional powers may conclude those of discharge or personal liability for non-compliance acts. These are normally proposals and final decisions on personal liability and sanctions are taken in a jurisdictional process. Personal liability can be measured by the extent of the participation of the person in a non-compliant (illegal, unnecessary, excessive, extravagant, unconscionable) transaction as indicated in the transactions documents that s/he signed.
- 224) In the report the auditor needs to explain the methods applied in determining whether each responsible person involved in administering, managing, utilizing or controlling public funds or assets is liable for the acts of non-compliance or not.

CONSIDERATIONS RELATED TO THE REPORTING OF SUSPECTED UNLAWFUL ACTS

Requirement

- 225) In conducting compliance audits, if the auditor comes across instances of non-compliance which may be indicative of unlawful acts or fraud, s/he shall exercise due professional care and caution and communicate those instances to the responsible body. The auditor shall exercise due care not to interfere with potential future legal proceedings or investigations.**

Explanation

- 226) While detecting potential unlawful acts, including fraud, is not the main objective of conducting a compliance audit, the auditor does include fraud risk factors in his/her risk assessments, and remains alert for indications of unlawful acts, including fraud, in carrying out his/her work.
- 227) The auditor may consider consulting with legal counsel or appropriate regulatory authorities. Furthermore, s/he may communicate their suspicions to the appropriate levels of management or to those charged with governance, and then follow up to ascertain that appropriate action has been taken. Because of the different mandates and organizational structures that exist internationally, it is up to the SAI to determine the appropriate action to be taken regarding instances of non-compliance related to fraud or serious irregularities.
- 228) A court of law can determine whether a particular transaction is illegal and constitutes a criminal offence. But SAIs with jurisdictional powers may also conclude that a particular transaction is illegal and may justify imposing sanctions on the responsible person and determining the reimbursements of funds, misappropriated assets, and undue or improper payments.
- 229) Although auditors do not determine if an illegal act constitutes a criminal offense or if civil liability has occurred, they do have a responsibility to assess whether the transactions concerned are in compliance with applicable laws and regulations and whether they constitute infringements that will lead the court to impose sanctions or reimbursement of undue or improper payments or of misappropriated assets.
- 230) SAIs with jurisdictional powers may communicate unlawful acts to the prosecution body who decides whether or not the case needs to be treated in a court of justice.
- 231) If suspicion of unlawful acts arises during the audit, the auditor may communicate this to the appropriate levels of management and those charged with governance. Those charged with governance are likely to be ministerial or administrative bodies higher up in the reporting hierarchy. Where appropriate and reasonable, the auditor may follow up and ascertain that management or those charged with governance have taken appropriate action in response to the suspicion, for example by reporting the incident to the relevant law enforcement authorities. The auditor may also report such incidents directly to the relevant law enforcement authorities.

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REQUIREMENTS RELATED TO FOLLOW-UP

Requirement

232) The auditor shall decide follow up on opinions/conclusions/recommendations of instances of non-compliance in the audit report when appropriate.

Explanation

233) An important role for a SAI in monitoring the action taken by the responsible party is to follow-up on the matters raised in an audit report. A plan for a follow-up is written after the report is published containing questions on whether the audited entity has adequately addressed the matters raised. Insufficient or unsatisfactory action by the audited entity may call for a further report by the SAI.

234) A follow-up process facilitates the effective implementation of corrective action and provides useful feedback to the audited entity, the user(s) of the audit report, the general public and the auditor for future audit planning.

235) The need to follow up previously reported instances of non-compliance will vary with the nature of the subject matter, the non-compliance identified and the particular circumstances of the audit. In some SAIs, including SAIs with jurisdictional powers, the follow-up may include issuing legally binding reports or judicial decisions. In audits carried out on a regular basis the follow-up procedures may form part of the subsequent year's risk assessment. This may include formal reporting by the auditor to the legislature, as well as to the audited entity or other appropriate bodies. Other follow-up processes may include reports, internal reviews and evaluations prepared by the audited entity or others and a follow-up audit.

236) Follow-up processes may be set out in the mandate of the SAI. Such processes may be constructive for the audited entity.