Module 1 - Assurance services framework

CPA Advanced Auditing and Assurance 2016 Notes

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<td>1. Engagement letter [p90]</td>
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<tr>
<td>1. Gained understanding of</td>
<td>1. Audit strategy: [p147] The auditor is to plan the audit so that it</td>
</tr>
<tr>
<td>entity and environment</td>
<td>will be performed in an effective manner. To reduce audit risk to an</td>
</tr>
<tr>
<td>2. Planned the audit</td>
<td>acceptably low level, this includes (ISA 300):</td>
</tr>
<tr>
<td>3. Undertaken initial risk</td>
<td>• Developing an overall strategy</td>
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<tr>
<td>assessment of material</td>
<td>• Developing an audit plan</td>
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<tr>
<td>misstatement</td>
<td>2. Risk analysis and assessment [p158]</td>
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<td>4. Prepared audit program</td>
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<td>• Detection risk [p85]</td>
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<td>• Fraud risk [p3027]</td>
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<td>• Materiality [p151]</td>
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<td>• Control environment [p161]</td>
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<td>• Strategic analysis [p177]</td>
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<td>• Analytical procedures [p185]</td>
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<td>Evidence gathering:</td>
<td>1. Tests of controls [p222]</td>
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<td>having identified the</td>
<td>• Sampling [p230]</td>
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<td>assertions containing a</td>
<td>2. Substantive tests [p232]</td>
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<td>risk of material</td>
<td>• Substantive analytical procedures [p232]</td>
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<td>misstatement, the auditor</td>
<td>• Tests of detail [p236]</td>
</tr>
<tr>
<td>undertakes audit procedures</td>
<td>• Sampling [p244]</td>
</tr>
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<td>to reduce this risk to</td>
<td>3. Final procedures</td>
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<td>an acceptable level via</td>
<td>• Subsequent events [p264]</td>
</tr>
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<td>selecting the most</td>
<td>• Going concern</td>
</tr>
<tr>
<td>efficient and effective</td>
<td>• Management representations [p266]</td>
</tr>
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<td>combination of tests of</td>
<td>1. Auditor’s report</td>
</tr>
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<td>controls and substantive</td>
<td>• Unmodified opinion (ISA 700 (revised)) [p298] and key audit matters</td>
</tr>
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<td>procedures.</td>
<td>(ISA 701) [p302]</td>
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<td>Modifications</td>
</tr>
<tr>
<td></td>
<td>i. Modified opinion (ISA 705 (revised))</td>
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<td>1. Qualified [p305]</td>
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<td></td>
<td>2. Disclaimer [p306]</td>
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<td>3. Adverse [p305]</td>
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<td>2. Other matter [p310]</td>
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<tr>
<td></td>
<td>• Key audit matter/emphasis of matter/other matter</td>
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<td>2. Other communications</td>
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<td>• Those charged with governance [p295]</td>
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<td>• Regulatory bodies [p294]</td>
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<td>• Shareholders [p292]</td>
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Assurance services framework

What is the definition of assurance engagement as provided by *The International Framework for Assurance Engagements*? [p16]

- An engagement in which an assurance 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.

What is the difference between 'auditing' and 'assurance'? [p15]

1. Auditing is a specific type of assurance engagement (subset of assurance engagements) that focuses on historical financial information.

What are the three categories for assurance services, what are the level of assurance provided, examples of these categories and the international standards governing the audit services? [p16, 21]

<table>
<thead>
<tr>
<th>Type of information</th>
<th>Historical financial information</th>
<th>Historical financial information</th>
<th>All other information</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Types of assurance services</strong></td>
<td>Audits</td>
<td>Reviews</td>
<td>Assurance engagements other than audits and reviews of historical financial information. May be future oriented and/or non financial.</td>
</tr>
<tr>
<td><strong>Level of assurance provided</strong></td>
<td>Reasonable</td>
<td>Limited</td>
<td>Reasonable or limited</td>
</tr>
</tbody>
</table>
| **Examples** | Audit of financial statements | Review of financial statements | 1. Prospective financial information  
2. Suitability report  
3. Greenhouse gas report  
4. Internal control report  
5. Performance information |
| **International Standards (Issued by IAASB)** | ISAs 100-999 International Standards on Auditing | ISREs 2000-2699 International Standards on Review Engagements | ISAEs 3000-3699 International Standards on Assurance Engagements |
| **Australian Standards** | ASA | ASRE | ASAE |
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What is the ISRS 4000-4699 International standards on Related Services? [p21]

- These are not for assurance engagements (in that they are not designed to offer a degree of assurance), but do utilise assurance-type, evidence-gathering procedures (eg. agreed procedures engagements to report factual findings).

What are the four stages of a financial statement audit and the issues at each stage? [p17]

1. Client acceptance: ethics, engagement letter
2. Planning: audit strategy, risk analysis and assessment
3. Evidence gathering: tests of controls, substantive tests, final procedures
4. Reporting: auditor’s report, other communication.

What is the objective of the auditor? [p82]

1. 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
2. To report on the financial statements, and communicate as required by the ISAs, in accordance with the auditor’s findings.
Regulation of Auditing and Auditing Standards

What are the roles of the following bodies IFAC, IASSB, IFIAR in auditing? [p19-20]

- IFAC (International Federation of Accountants): global organization for the accountancy profession where members are the associations of professional accountants from around the world. In charge of establishing the International Ethics Standards Board for Accountants (IESBA) to develop the Code of Ethics for Professional Accountants
- IAASB (International Auditing and Assurance Standards Board): an independent standard-setting body that serves the public interest by setting high-quality international standards for auditing, quality control, review, other assurance, and related services, and by facilitating the convergence of international and national standards
- IFIAR (International Forum of Independent Audit Regulators): Oversight of the auditing profession by independent audit regulatory authorities from different countries.

What is the hierarchy, in order of compliance, of IASSB pronouncements? [p20]

1. IESBA Code of Ethics for Professional Accountants
2. ISQCs 1-99 International Standards on Quality Control

Which bodies are involved in audit regulation in Australia? [p21-22]

1. FRC (Financial Reporting Council): Independent statutory agency to oversee the accounting and auditing standards-setting process. Include appointments to the AUASB
2. ASIC (Australian Securities and Investment Commission): Independent Commonwealth body to carry out the work under the Corporations Act 2001 (Cwlth) including oversight of the auditing profession (registration of auditors, enforcement of rules regarding auditor independence, use of auditing standards and inspection of audit firms)
3. APESB (Australian Professional and Ethical Standards Board): Funded by the professional accounting bodies for setting the ethical standards in Australia and quality control ethical conduct and compliance with auditing and assurance standards.
4. AUASB (Australian Auditing and Assurance Standards Board): Consider revisions and improvements to pronouncements initiated by the IAASB

Are the Australian Auditing Standards (ASA) identical to the International Auditing Standards (ISA)? [p22]

- No, differences may arise to accommodate the requirements of Australian legislation or have additional requirements to those found in the internal standards which are prefixed by Aus x.x.
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- Eg. ASA 101 Preamble to *Australian Auditing Standards* has no international equivalent and outlines how the AUASB intends the Australian standards to be understood, interpreted and applied

What are the sections in the each ASA? [p22]

1. Introduction (purpose, scope and subject matter)
2. Objectives
3. Definitions
4. Requirements
5. Application and other explanatory material (which may include examples of appropriate procedures)

What are guidance statements issued by the AUASB used for? [p22]

- Include explanations and suggestions that help practitioners comply with AUASB standards

Only auditing standards, as opposed to auditing and assurance standards for other purposes, have the 'force of the law'. What do auditing standards include? [p23]

1. All the ASAs
3. ASQC 1 *Quality Control for Firms that Perform Audits and Review of Financial Reports, Other Financial Information, and Other Assurance Engagements*

What are some Australian-specific review requirements about when to apply each standard? [p23]

<table>
<thead>
<tr>
<th>International Standards on Review Engagements</th>
<th>Australian Standards on Review Engagement</th>
</tr>
</thead>
<tbody>
<tr>
<td>ISRE 2400 when the practitioner is not the auditor of the entity, undertakes an engagement to review the financial statements</td>
<td>ASRE 2415 (no international equivalent) which describes a three-tiered differential reporting framework and describes how to select ASRE 2410 and ASRE 2400 for conducting a review</td>
</tr>
<tr>
<td>ISRE 2410 when the practitioner is the entity's auditor reviews interim financial information</td>
<td>ASRE 2419 when the auditor has conducted the audit of the previous report and has gained an understanding of the entity and its environment by complying with the auditing standards</td>
</tr>
<tr>
<td></td>
<td>ASRE 2400 when the auditor has not conducted an audit or the previous financial</td>
</tr>
<tr>
<td>report and does not have an understanding of the entity and its environment.</td>
<td></td>
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</tbody>
</table>
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International Framework for Assurance Engagements

What is the Australian equivalent of the Framework by IAASB? [p22]

- The Australian Framework for Assurance Engagement (Australian Framework), which conforms with the international version with minor differences

What is the Framework used for and what are the matters discussed? [p24]

- Used to help understand when the ISAs, ISREs, ISAEs and ISRSs apply
- It is not a standard and does not include any requirements for performance
- Matters discussed include
  1. Ethical principles
  2. Quality control
  3. Definition of assurance engagements
  4. Reasonable and limited assurance engagements
  5. Attestation and direct engagements
  6. Elements of an assurance engagement (three-party relationship, underlying subject matter, criteria, evidence, assurance report)
Ethical Principles

Who needs to comply with APES 110 Code of Ethics for Professional accountants (the Code)? [p25]

- ASA 102 states that auditors, assurance practitioner, engagement quality control reviewer and the firm shall comply with the Code.

What are the fundamental principles of the Code? [p25]

1. Integrity [p25]: Straightforward, honest, trustworthy, honourable, reliable and courageous
2. Objectivity [p25]: Impartial attitude to work avoid prejudice, bias, conflict of interest or undue influence that may compromise professional and business judgements
3. Professional Competence and due care [p25]:
   a. Maintain the professional knowledge and skills required (qualification and CPD)
   b. Act with due care in accordance with applicable technical and professional standards. Act timely and carefully and decline job unless have necessary skills.
4. Confidentiality [p25]: Not disclose information to third parties without proper authority, unless a legal or professional right or duty to disclose.
5. Professional behaviour [p26]: Comply with relevant laws and regulations and avoid any action that discredits the profession.

What are the threats to compliance with the fundamental principles of the Code? [p26]

1. Self-interest: financial or other interests
2. Self-review: previous judgement re-evaluated by the person or firm responsible for that judgement
3. Advocacy: Promote or represent client
4. Familiarity: Long or close relationship with client resulting in sympathy
5. Intimidation: Deterred from acting objectively due to actual or perceived threats

Where there are threats members must apply safeguards to eliminate or reduce them to an acceptable level or decline or discontinue providing the service. What are the safeguards? [p26]

1. Safeguard by the profession, legislation or regulation
2. Safeguard in the work environment of the assurance client
3. Safeguards in the work environment of the audit firm

What are the specific ethical issues arising from professional accountants in public practice? [p27]

1. Professional appointment [p27]:

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a. (Additional requirement for auditors) If the auditor has been an officer or audit-critical employee of the proposed client within the 12 months immediately before the proposed audit period, accepting an appointment is not permitted.

b. (Additional requirement for auditors) An accountant who is asked to replace an existing auditor must request the prospective client's permission to communicate with the existing auditor. If permission is not granted, the accountant should decline the appointment.

2. Conflict of interest [p27]:

3. Second opinions [p28]:
   a. If fees generated by an assurance client exceed 15% of the firm's total fees, an additional independent professional accountant must review the work done and the documentation of that review should be delivered to the engagement partner's professional body.

4. Fees and other types of remuneration [p28]:

5. Gifts and hospitality [p28]:

6. Independence [p28]: This is the cornerstone of the auditing and assurance profession. The Code requires independent both of mind and in appearance
   a. Mind/Fact: accountant must act with integrity, and exercise objectivity and professional scepticism.
   b. Appearance: a reasonable and informed third party would not think that a member's integrity, objectivity or professional scepticism has been compromised.

What are the three parts of the framework for audit quality as described in A Framework for Audit Quality: Key Elements That Create and Environment for Audit Quality? [p34]

1. Part 1 is the input, process and output to quality audits
   1. Inputs: exhibiting appropriate values, ethics, attitudes, sufficiently knowledgeable, skilled, experience and having sufficient time to perform work
   2. Process: auditors applying rigorous audit process and appropriate quality control procedures that comply with laws, regulations and applicable firm and national standards
   3. Outputs: Outputs from auditor, audit firm, the entity and audit regulators including independent auditor's report, firm's transparency report, management letter to audit committee.

2. Part 2 is the interactions between the various participants in the financial reporting supply chain: management, those charged with governance, regulators, users and auditors.

3. Part 3 are the 10 contextual factors:
   1. Business practices and commercial law
   2. Laws and regulations relating to financial reporting
   3. The applicable financial reporting framework
   4. Information systems
   5. Corporate governance
   6. Broader cultural factors
   7. Audit regulation
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8. Litigation environment
9. Attracting talent
10. Financial reporting timetable
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Quality control

What is ISQC 1 (ASQC 1) and how does it differ from ISA 220? [p30]
- ISQC 1 establishes basic principles and essential procedures for firms.
- The difference between ISA 220 is that it relates to a specific engagement while ISQC 1 is broader and relates to the audit firm as a whole.

What is the basic purpose of ISQC 1? [p97]
- To establish a system of quality control designed to provide reasonable assurance that:
  a. the firm and its personnel comply with professional standards and applicable legal and regulatory requirements
  b. reports issued by the firm or engagement partners are appropriate in the circumstances.

Note that national requirements must be at least as demanding as ISQC 1.

According to ISQC 1, what are the six areas where firms should have quality control (QC) in place? [p30]
1. Leadership responsibilities [p30]:
   - Operational responsibility rests with a person with appropriate experience and ability
   - Firm should develop, document and implement appropriate QC procedures and a formal code of conduct
   - Overriding commitment to quality above commercial considerations such as work is not limited to a budget but must be determined by the assessed risk.

2. Ethical requirements [p31]:
   - Firm to develop, document and implement policies and procedures to ensure ethical behaviour.
   - Have systems that support ethical behaviour like databases to match staff disclosures with a prohibited securities list.
   - Tracking the firm's performance in accordance with the auditor rotation requirements of the Corporations Act.

3. Acceptance and continuance of client relationships [p31]:
   - An assurance firm must
     i. Consider the integrity of each client
     ii. Determine that it is competent to perform the engagement
     iii. Determine that it can comply with the Code, including especially those matters related to independence.
   - Use a risk check list

4. Human resources [p31]: