

ACF3000

AUDITING & ASSURANCE

INTRODUCTION AND OVERVIEW OF AUDIT ASSURANCE

ASSURANCE ENGAGEMENT

Assurance engagement is an engagement in which an assurance practitioner aims to obtain sufficient appropriate evidence in order to express a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the measurement and evaluation of an underlying subject matter against criteria.

- Involves an auditor arriving at an opinion about some information being provided by their client to third party
- Financial audit is a type of assurance engagement
- This engagement involves an auditor arriving at an opinion about the truth and fairness of the report
- Audit report is addressed to the shareholders of the company being audited

TYPES OF ASSURANCE SERVICES

Assurance services include financial report auditors, compliance audits, performance audits, comprehensive audits, internal audits, and assurance on corporate social responsibility disclosures.

FINANCIAL REPORT AUDIT	Engagement designed to express opinion about whether report is prepared in all material aspects in accordance with financial reporting framework
COMPLIANCE AUDIT	Involves gathering evidence to ascertain whether rules, policies, procedures, laws and regulations have been followed (tax audit)
PERFORMANCE AUDIT	Refers to the economy, efficiency and effectiveness of an organisation's activities. Usually done by internal auditors or can be outsourced to external auditors
COMPREHENSIVE AUDIT	Combines elements of financial report, compliance and performance audit. Often occurs in public sector
INTERNAL AUDIT	Provides assurance about various aspects of an organisation's activities. Often contains elements of performance audits, compliance audits, internal control assessment and reviews
CSR ASSURANCE	Includes voluntary reporting about environmental, employee and social subject matters. Incorporates both financial and non-financial information. Auditor must consider environmental issues on their clients' financial reports even if reports do not include any disclosures

DIFFERENT LEVELS OF ASSURANCE

Different levels of assurance include reasonable assurance (highest level of assurance), limited assurance or no assurance. Reasonable assurance is provided on an audit of a company financial report. Limited assurance is provided on a review of a company's half-year financial report. No assurance is provided on an agreed upon procedures engagement.

LEVEL OF ASSURANCE	EXAMPLE		EXPRESSION
REASONABLE The highest level of assurance but not absolute assurance on the reliability of the subject matter	Financial report audit	The auditor has conducted sufficient tests & obtained sufficient appropriate evidence to conclude positively that the information that is assurance is (is not) reliable	Positive
LIMITED Moderate assurance on the reliability of the subject matter	Review of a company's half year financial report	The auditor has done adequate work to report whether or not anything came to their attention that would lead them to believe that the information that is assurance is not true and fair	Negative
NO ASSURANCE	Agreed upon procedures engagement	The auditor does not report an opinion – merely report on the findings & facts of their findings. The client determines the nature, timing and extent of evidence gathered and then draws their own conclusions about these findings	No assurance given

DIFFERENT AUDIT OPINIONS

- **UNMODIFIED REPORT**
- **MODIFIED REPORT** that does not affect the auditor's opinion (emphasis of matter opinion)
- **MODIFIED REPORT** that does affect the auditor's opinion (qualified opinion, adverse opinion or disclaimer of opinion)

An unmodified opinion (unqualified opinion/clean opinion) depicts that the financial report is true and fair, presents fairly and the financial position of the company complies with standards and regulations.

A modification that does not affect the auditor's opinion is an **emphasis on matter** paragraph. Modifications that do affect the auditor's opinion are a **qualified opinion**, **adverse opinion**, or **disclaimer of opinion**.

NATURE OF MATTER GIVING RISE TO THE MODIFICATION	AUDITOR'S JUDGEMENT ABOUT THE PERVASIVENESS OF THE EFFECTS/POSSIBLE EFFECTS ON THE FINANCIAL REPORT	
	Material but not pervasive	Material and pervasive
Financial report is materially misstated	Qualified opinion	Adverse opinion
Inability to obtain sufficient appropriate audit evidence	Qualified opinion	Disclaimer of opinion

- A qualified opinion is given when there are reservations about the truth and fairness of the financial statements. This can include a qualified or 'except for' opinion. This is when issue(s) are material but not pervasive
- Adverse opinion would arise when the financial report is misstated and is material and pervasive
- Disclaimer of opinion would arise when there is an inability to obtain sufficient appropriate audit evidence and is material and pervasive

When something is material, it refers to a single item that is misstated, can be isolated, and does not have widespread effects, so only that part of the statement cannot be relied upon. When something is pervasive, it refers to a single item or multiple items that are misstated, cannot be isolated, and have widespread effects on the financial statements, and so very little of the statement can be relied upon

DIFFERENT ROLES OF THE PREPARER AND THE AUDITOR, AND THE DIFFERENT FIRMS THAT PROVIDE ASSURANCE SERVICES

It is the responsibility of a company's governing body to ensure that their financial report is relevant, reliable, comparable, understandable, and true and fair. It is the responsibility of the auditor to form an opinion on the truth and fairness or fair presentation of the financial report. In doing so the auditor must maintain their professional scepticism and utilise professional judgement and due care. The different firms that provide assurance services include the Big-4 international firms, the mid-tier national firms (with international links), local and regional firms, and consulting firms that tend to specialise in assurance of CSR and environmental disclosures.

DEMAND FOR AUDIT AND ASSURANCE SERVICES

Financial report users include investors (shareholders), suppliers, customers, lenders, employees, governments and the general public. These groups of users demand audited financial reports due to their remoteness from the entity, accounting complexity, competing incentives between them and the entity's managers, and their need for reliable information on which to base decisions. The theories used to describe the demand for audit and assurance services are agency theory, the information hypothesis and the insurance hypothesis.

DIFFERENT REGULATORS AND REGULATIONS SURROUNDING THE ASSURANCE PROCESS

- Financial Reporting Council (FRC)
- Auditing and Assurance Standards Board (AUASB)
- Accounting Professional and Ethical Standards Board (APESB)
- Australian Securities and Investments Commission (ASIC)
- Australian Securities Exchange (ASX)
- Companies Auditors and Liquidators Disciplinary Board (CALDB)
- Chartered Accountants Australia & New Zealand (CAANZ)
- CPA Australia
- Institute of Public Accountants (IPA)
- Auditing standards and pronouncements
- Corporations Law
- CLERP 9.

AUDIT EXPECTATION GAP

The audit expectation gap occurs when there is a difference between the expectations of assurance providers and financial report or other users. The gap occurs when user beliefs do not align with what an auditor has actually done.

- Limitations to the audit include: there is no guarantee that the financial report is free from error or fraud; the nature of audit procedures and processes are required to be performed within a reasonable period and at a reasonable cost; and judgement is required in the process of preparation of the financial statements.
- Can be caused by unrealistic expectations including: the auditor providing a complete assurance; the auditor guaranteeing future viability of the entity; an unqualified opinion denotes complete accuracy; and the auditor will fund all frauds. We know these cannot be met by the auditor.
- The expectation gap can be reduced by: auditors performing their duties appropriately; undertaking peer reviews of work performed; reviewing and updating auditing standards; educating the public; enhanced reporting explaining audit processes and levels of opinion auditors provide to the entity; and greater attention to the risk of material fraud occurring.

ETHICS, LEGAL LIABILITY AND CLIENT ACCEPTANCE

FUNDAMENTAL PRINCIPLES OF PROFESSIONAL ETHICS

Fundamental principles of professional ethics include:

- **Integrity:** being straightforward and honest
- **Objectivity:** not allowing personal feelings/prejudices to influence judgement
- **Professional competence and due care:** maintaining knowledge and skill at an appropriate level
- **Confidentiality:** not sharing sensitive information
- **Professional behaviour:** upholding reputation of the profession

AUDITOR INDEPENDENCE

Independence is the ability to make a decision that is free from bias, personal beliefs and client pressures. An external auditor must not only be independent of the client, they must also appear to be independent of their client. Threats to auditor independence include self-interest, self-review, advocacy, familiarity and intimidation threats.

THREAT	DEFINITION	EXAMPLES
SELF-INTEREST THREAT	Financial interest in a client	Bank account held with the client Shares owned in the client Loan to/from the client (unpaid audit fees amount to loan) Fee dependence Fees from client form significant portion of all fees Close business relationship with client
SELF-REVIEW THREAT	Audit of their own work or work done by others in their firm	Assurance team member recently been employee/director of client Preparing info for client that is then assured Performing services for client that are then assured
ADVOCACY THREAT	Auditor acting on behalf of their client	Encouraging others to buy client's shares/bonds Representing client in negotiations with third party Representing the client in legal disputes
FAMILIARITY THREAT	Close relationship between the auditor and their client	Long association between assurance firm/client Acceptance of gifts by members of assurance team from client (other than minor tokens) Acceptance of hospitality of assurance team from client (other than minor gestures)
INTIMIDATION THREAT	Auditor feels threatened by their client	Threat that client will use different firm next year Undue pressure to reduce audit hours to reduce fees paid

Safeguards to audit independence include the code of ethics, legislation, the establishment of audit committees by clients, client acceptance and continuation procedures, partner rotation policies and education within accounting firms.

Lack of auditor independence impacts on credibility and reliability of the financial report. The auditor must be (ability to be independent) and seen to be (belief that independence is achieved), independent.