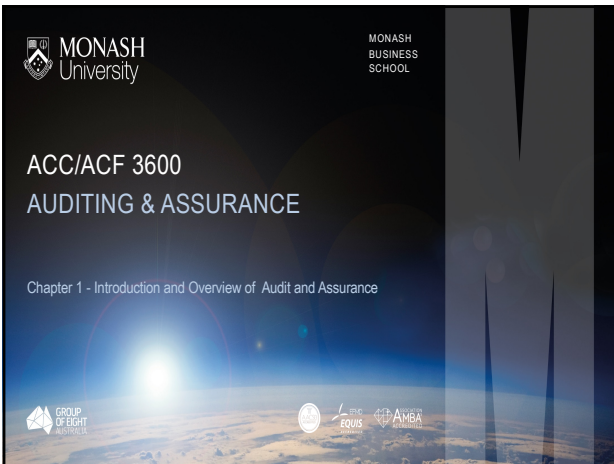




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LEARNING OBJECTIVES

After studying this presentation you should be able to:

- 1.1 describe an assurance engagement
- 1.2 discriminate between different types of assurance services
- 1.3 discriminate between different levels of assurance
- 1.4 categorise different audit opinions
- 1.5 discriminate between the different role of the preparer and the auditor, and discuss the different firms that provide assurance services
- 1.6 justify the demand for audit and assurance services
- 1.7 compare the different regulators and regulations surrounding the assurance process
- 1.8 categorise the audit expectation gap.

Adapted from Moroney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.), Wiley

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AUDITING AND ASSURANCE DEFINED

An **assurance engagement** is defined as:

An assurance engagement (or service) is defined as '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 or evaluation of an underlying **subject matter** against **criteria**.'

Adapted from Moroney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.), Wiley

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AUDITING AND ASSURANCE DEFINED

'intended users' - the people for whom the assurance practitioner prepares their report.

Example: **shareholders, creditors, employees**

'responsible party' - the person or organisation responsible for the preparation of the subject matter.

Example: **company management**

'subject matter' - that which the assurance practitioner is expressing a conclusion on.

Example: **financial reports**

'criteria' - the rules or principles by which the subject matter is being evaluated.

Example: **Accounting standards and interpretations and Corporations laws**

Adapted from Monney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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DIFFERENT ASSURANCE SERVICES

The most common assurance services are:

- Financial report audit
- Compliance audit
- Performance audit
- Comprehensive audit
- Internal audit
- CSR

Adapted from Monney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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DIFFERENT ASSURANCE SERVICES

The most common assurance services are:

1. **Financial report audits:**
an engagement designed to express an opinion about whether the report is prepared in all material respects in accordance with a financial reporting framework (ASA 200, para. 11; ISA 200, para 11)
- **Limitations of an audit:**
 - 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** (ASA 200, ISA 200).
 - **Judgement is required** in the process of preparation of the financial statements.

Adapted from Monney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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DIFFERENT ASSURANCE SERVICES

2. Compliance audit:

- Involves gathering evidence to ascertain whether **rules, policies, procedures, laws** and **regulations** have been followed.

- A **tax audit** is an example of a compliance audit.

3. 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.

4. Comprehensive audit:

- Combines elements of financial report audit, compliance audit and performance audit.
- Often occur in the **public sector**.

Adapted from Monney, Robin, et al. (2017). Auditing: A practical approach (3rd ed.), Wiley

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DIFFERENT ASSURANCE SERVICES

5. Internal audit:

- Provides assurance about **various aspects** of an organisation's activities.
- Often contain elements of **performance** audits, **compliance** audits, **internal control** assessments and reviews.

6. Corporate social responsibility (CSR) assurance:

- Includes voluntary reporting about **environmental, employee** and **social** subject matter.
- Incorporates both **financial** and **non-financial** information.
- Quantification of green gas emissions (GHG): Assurance Engagements on Greenhouse Gas Statements (ASAE 3410)

Adapted from Monney, Robin, et al. (2017). Auditing: A practical approach (3rd ed.), Wiley

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DIFFERENT LEVELS OF ASSURANCE

LEVEL OF ASSURANCE	EXAMPLE		THE ASSURANCE EXPRESSION
REASONABLE Highest level of assurance but not absolute assurance on the reliability of the subject matter	Financial Statement Audit	The auditor has conducted sufficient tests and obtained appropriate and sufficient evidence to conclude positively that the information that is assured is (or is not) reliable	Positive
LIMITED Moderate assurance on the reliability of the subject matter	Review of a company's half-year financial report	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 assured is not true and fair.	Negative
NO ASSURANCE	Agreed-upon procedures engagement	The auditor does not report an opinion – merely report on the findings and the 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

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DIFFERENT AUDIT OPINIONS

Unmodified:

- Also known as an **UNQUALIFIED OPINION** or **clean opinion** – as in a 'clean bill of health'.
- Financial report is true and fair, presents fairly the financial position of the company, information complies with AAS and Corp Act.

Modified:

- Modifications that **do not affect** the auditor's opinion:
 - ❑ **Emphasis of matter**
- Modifications that **affect** the auditor's opinion:
 - ❑ **Qualified Opinion**
 - ❑ **Adverse opinion**
 - ❑ **Disclaimer of Opinion**

Adapted from Monney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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DIFFERENT AUDIT OPINIONS

- Other modified reports are qualified (ASA 705). A **qualified opinion** is given when there are **reservations** about the 'truth and fairness' of the financial statements.
- Can include a qualified or '**except for**' opinion. This is when issue(s) are **material but not pervasive**.
- **Adverse opinion** would arise when 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**.

Adapted from Monney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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AUDIT REPORT STRUCTURE (ASA 700)

Report on the Audit of the Financial Report

Opinion

- **True and fair view of financial position / performance**
- **Compliance with Corporations Regulations 2001**

Basis for Opinion

- **ASA**
- **Independence**

Key Audit Matters

- **Matters of most significance in the audit**

Other Information

- **Unaudited Information in the annual report**

Adapted from ASA 700

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AUDIT REPORT STRUCTURE (ASA 700)

Responsibilities of the Directors for the Financial Report

- Preparation of the financial report

Auditor's Responsibilities for the Audit of the Financial Report

- Obtain reasonable assurance

Report on the Remuneration Report

Opinion on the Remuneration Report

- Compliance with section 300A of the Corporations Act 2001

Responsibilities

- Directors: preparation of the remuneration report
- Auditors: express an opinion

Adapted from ASA 700

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PREPARERS AND AUDITORS

It is the responsibility of those **charged with governance** to prepare the financial statements. The information should be:

- Relevant
- Reliable
- Comparable
- Understandable
- True and fair

Adapted from Monney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.), Wiley

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PREPARERS AND AUDITORS

Auditor has responsibilities relating to the audit:

- **Professional scepticism**: maintaining **independent** of the entity and having a **questioning mind** to thoroughly investigate all evidence presented.
- **Professional judgement**: use of **judgement** based on level of **expertise, knowledge** and **training** obtained by the auditor.
- **Due care**: being **diligent, applying standards** and **documenting** each stage of the audit process.

Adapted from Monney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.), Wiley

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PREPARERS AND AUDITORS

Assurance services are provided by **accounting** and **consulting firms**.

There are three tiers of accounting assurance providers

- **First-tier**
- **Mid-tier**
- **Other**

Adapted from Monney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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DEMAND FOR AUDIT AND ASSURANCE SERVICES

- The users of the financial statements are not limited to the **shareholders** or **owners** of the business.

- Other users include:

- **Potential investors**
- **Suppliers**
- **Customers**
- **Lenders**
- **Employees**
- **Government**
- **Public**

Adapted from Monney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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SOURCES OF DEMAND FOR AUDIT & ASSURANCE SERVICES

1. **Remoteness**
users do not have access to information themselves.
2. **Complexity**
users do not have knowledge to be able to make disclosure choices.
3. **Competing incentives**
users may find it difficult to identify when the incentives of management have been over-represented.
4. **Reliability**
as decisions are being made based on information presented, it is important that it be reliable.

Adapted from Monney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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THEORETICAL FRAMEWORKS

1. Agency theory
2. Information hypothesis
3. Insurance hypothesis

Adapted from Moroney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.). Wiley

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DEMAND IN A VOLUNTARY SETTING

- It is becoming more common for companies to voluntarily disclose CSR information
- This demand is driven by a variety of stakeholders
- Entities are not required to disclose CSR activities or to have them assured
- Assurance enhances the credibility of CSR disclosures

Adapted from Moroney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.). Wiley

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THE ROLE OF REGULATORS AND REGULATIONS

- FINANCIAL REPORTING COUNCIL (FRC)
- AUDITING AND ASSURANCE STANDARDS BOARD (AUASB)
- ACCOUNTING PROFESSIONAL AND ETHICAL STANDARDS BOARD (APESB)
- INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD (IAASB)
- AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION (ASIC)
- AUSTRALIAN SECURITIES EXCHANGE (ASX)
- COMPANIES AUDITORS AND LIQUIDATORS DISCIPLINARY BOARD (CALDB)
- PROFESSIONAL BODIES (CPA AUSTRALIA, CA ANZ, IPA)

Adapted from Moroney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.). Wiley

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REGULATION

CORPORATIONS ACT

- Provides guidance on conducting audit of financial reports.
- This includes that certain accounts need to be audited (s. 301,) the audit report stating whether it is true and fair & in accordance with accounting standards (s. 307,) standards must be applied (s. 307A,) retention of audit working papers (s. 307B,) and independence declaration (s. 307C.)

Adapted from Monney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.). Wiley

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REGULATION

CLERP 9

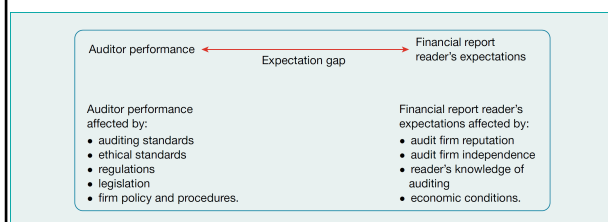
- Significant changes brought about from 1 July 2004 including auditing standards having 'force of law.'
- Other changes include:
 - » Disclosure of non-audit services provided by auditor.
 - » Enhanced independence and employment requirements.
 - » Partner rotation

Adapted from Monney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.). Wiley

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AUDIT EXPECTATION GAP



Adapted from Monney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.). Wiley

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AUDIT EXPECTATION GAP

- The audit expectation gap is the difference between the expectations of assurance providers and financial report or other users.
- Can be caused by unrealistic user expectations including:
 - The auditor providing a complete assurance.
 - The auditor guaranteeing future viability of entity.
 - An unqualified opinion denotes complete accuracy.
 - The auditor will find all frauds.

Adapted from Moroney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.). Wiley

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AUDIT EXPECTATION GAP

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.
- Greater attention to the risk of material fraud occurring.

Adapted from Moroney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.). Wiley

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Question 1

You are the auditor in charge of ABC company. During the audit of the 2017 annual report, one office of ABC company was destroyed by fire. Because of the fire, you are unable to find out some sales invoices (about 1% of total sales) and there is no backup in the company. Without the invoices, you are also unable to contact customers for confirmation purposes. You have access to the remaining 99% of invoices, and you believe there is no material misstatement in these invoices.

Question: In this case, which type of audit opinion you would issue?

Adapted from Moroney, Robyn, et al. (2017). Auditing: A practical approach (3rd ed.). Wiley

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Question 2

You received some red envelopes containing money from your family during the Chinese New Year. You want to invest the money in the stock market. However, you don't know which company to invest in. You search for information of several potential investment targets. In the end, you choose ABC company because it has improved its performance during the past few years. In addition, this company is audited by Monash CPA Firm, and you believe that Monash CPA Firm has a good reputation and audit quality. Therefore, you believe that the financial statements of ABC Company are free from bias.

Question: Which theory best explains this case?

Adapted from Moroney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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Question 3

More and more countries have adopted International Financial Reporting Standards (IFRS). People believe that by using the same (or similar) financial reporting standards, financial statements can become more useful.

Question: Why does using IFRS increase the usefulness of financial statements? Which characteristic is addressed?

Adapted from Moroney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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Question 4

Question a: In times of economic recession would you expect the demand for audits to increase or decrease?

Question b: In times of economic recession would you expect clients to shift from large (Big-4) auditors to mid-tier auditors, or from mid-tier auditors to Big-4 auditors? Why or why not?

Question c: Do you expect the difference in audit quality between Big-4 and other auditors to be higher or lower when the legal environment is better?

Adapted from Moroney, Robyn, et al. (2017). *Auditing: A practical approach* (3rd ed.). Wiley

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