



CAS meeting Brasília 18th–19th of September 2013

Issue paper II

CAS maintenance strategy 2013–2016

1. Introduction

At INCOSAI in China in October 2013 a new set of fundamental principles for public sector auditing is being endorsed, including the new ISSAI 400 *Fundamental Principles for Compliance Auditing*. The new level 3 ISSAIs provide a milestone in the development of public sector auditing and for the work of CAS. This issue paper outlines the background for the maintenance strategy to be adopted by CAS at the meeting in Brasília on the 18th–19th of September 2013 in light of the strategy and maintenance frequency already adopted by CAS, the outcome of the harmonization project and the lessons learned from the implementation of the ISSAI 4000 series across INTOSAI. Further, it includes the main strategic crossroads for the committee to choose a path forward in the maintenance of the Compliance Audit Guidelines and the suggested priorities regarding their contents development.

2. Background

In addition to providing a new foundation for the ISSAIs and a common language for public sector auditing, the fundamental principles for public sector auditing explain how the ISSAIs can be referred to and the authority of level 3 in relation to level 4. The new fundamental principles can be used as a basis for developing authoritative standards, one of the options for a SAI being to adopt the general auditing guidelines (ISSAI 4000 series) as authoritative standards. The decision that the Compliance Audit Guidelines may be applied as authoritative standards is reflected in a new set of drafting conventions for Auditing Guidelines¹, stating the following:

- The ISSAIs should support the general requirements which are defined by level 3 of the ISSAI framework, including referring to the relevant principles and using the same terminology.
- The ISSAIs should distinguish between requirements and further guidance, and the word "shall" is to be used to indicate a requirement.

These decisions of the harmonization project forms the point of departure for the maintenance of the ISSAI 4000 series.

At the CAS meeting in Lithuania in 2012 CAS identified the following aims of the strategic period 2012–2016:

1. Establishing a strong professional environment for Compliance Audit in the public sector
2. Presenting ISSAI 400 for INCOSAI 2013
3. Presenting an updated and coherent ISSAI 4000 series for INCOSAI 2016

¹ See additional paper 3



3. Main strategic crossroads

3.1 The structure of the ISSAI 4000 series

3.1.1 Existing structure of ISSAI 4000 series

Historically, the development of the ISSAI 4000 series started with the need to identify the contents and processes of the broader perspective of audits performed by SAIs in relation to the audit of the financial statements when INTOSAI made the decision to adopt and add on to the ISAs of IFAC. The further process discovered that many SAIs also performed Compliance Audit as a separate audit. This is the reason behind the present structure of the ISSAI 4000 series, a high level guideline uniting a variety of audit practices across INTOSAI.

The existing Compliance Audit Guidelines consists of three documents:

- ISSAI 4000 *General Introduction*
- ISSAI 4100 *For Audits Performed Separately from the Audit of Financial Statements*
- ISSAI 4200 *Compliance Audit Related to the Audit of Financial Statements*

The committee has been presented several drafts of a proposed ISSAI 4300 *Compliance Audit in the Context of Courts of Accounts*. ISSAI 400 mentions yet another option as how a compliance audit can be performed: *Compliance Auditing in combination with performance auditing*.²

The development of the Compliance Audit Guidelines has shown that compliance auditing is performed in a series of different combinations and variations within INTOSAI, all with their specific needs and issues. Yet, the major achievement of the work of CAS has been the ability to find new concepts and a common ground identifying the basic steps of compliance auditing as performed by SAIs.

In looking at the existing structure of the Compliance Audit Guidelines, the known needs and issues to be addressed would lead to an extension of the ISSAI 4000 series with yet another two documents, an ISSAI 4300 for compliance audits performed in courts and an ISSAI 4400 for compliance audit performed related to performance audit.

Comments of the chair

The existing ISSAI 4100 and ISSAI 4200 are documents most similar, where only approximately 10% of the substantial contents differ. Extending the number of documents to encompass further needs would lead to a number of documents, seemingly similar, yet differing.

The implementation of the ISSAI 4000 series has shown the necessity for the standard to communicate in a simple and clear manner what is the audit process and what are the requirements of an audit. In this context, there is a need to explore a new structure, within the document and between documents. The new structure should communicate clearly the basic common requirements of compliance auditing and distinguish the process steps and requirements when it is performed in its combinations and variations.

Furtheron, the development of the level 3 ISSAI has established compliance auditing unequivocally as one of the three audit types of public sector auditing. ISSAI 100 explains how the audit types can be

² ISSAI 400 para. 26



combined in order for a SAI to fulfill its mandate.³ Hence, the main need when transforming the ISSAI 4000 series into authoritative standards is to communicate what compliance auditing is in its own right and less focus on its variations and combinations in the main structure and title of the ISSAI 4000 series.

3.1.2 One common authoritative standard on compliance auditing: ISSAI 4000

When developing the ISSAI 400 the CAS harmonization team worked on the basis of the existing compliance audit guidelines in order to identify the basic principles of the audit process, where "should" statements indicate the requirements to become "shall-statements" on the auditor throughout the audit process on level 4. These principles have been identified at an even higher level than the ISSAI 4000 series, encompassing both compliance auditing conducted separately, in relation with the audit of financial statements and in combination with performance auditing. They have also been developed so as to encompass attestation and direct reporting engagements⁴ and to cover audits both giving opinions and conclusions.⁵ Hence, ISSAI 400, gives CAS a good point of departure for developing one common authoritative standard on compliance auditing.

Comments of the chair

It is the opinion of the chair that the committee should explore a new possible structure of the ISSAI 4000 series, starting out with one common authoritative standard on compliance auditing expressing the basic requirements of all compliance audits: an ISSAI 4000.

This would lead the committee into reconsidering how to structure the ISSAI 4000 series to encompass the relevant combinations and variations of compliance auditing within INTOSAI:

- in relation with the audit of financial statements and in combination with performance auditing
- in the Context of Courts of Accounts
- as attestation engagements and direct reporting engagements
- giving reasonable and limited assurance
- giving opinions and conclusions.

3.2 The number of requirements and volume of guidance in the standards

In the maintenance of the ISSAI 4000 series, one of the main task of CAS is to translate the "should" statements of ISSAI 400 into "shall" requirements in the ISSAI 4000 series. The second strategic crossroads for the committee to choose a path forward is hence to give direction as to the number of requirements and volume of guidance in the updated ISSAI 4000 series.

At present there is a vast difference between the number and volume of requirements in the level 4 ISSAIs - comparing the ISSAI 1000 series, which contains around 1000 pages with the number and volume of requirements in ISSAI 3100, containing nine pages. CAS needs to choose its pathway somewhere in between these alternatives.

³ ISSAI 100 paragraphs 16, 21 and 23

⁴ ISSAI 100 paragraphs 29 and 30

⁵ ISSAI 400 paragraph 59



The number of requirements and volume of guidance needs to be sufficient to cover a professional audit process and at the same time make the standard accessible for implementation.

Comments of the chair

In the view of the chair, a public sector standard should be accessible in volume and contain the number of requirements that makes it realistic for SAIs to comply with them. Which these requirements have been thoroughly considered through the making of the ISSAI 4000 series and ISSAI 400. Hence, the number of requirements in departing the maintenance of the ISSAI 4000 series should be limited to approximately the number of principles in ISSAI 400. The chair considers the volume of guidance of a common authoritative standard on compliance auditing to be developed into approximately the same volume as in the existing ISSAI 4000 series.

The attached appendix 1 gives a draft example of what this extent and volume would look like in one particular requirement.

3.3 Alternatives as how to address the specific issues of compliance auditing

Yet remains the issue of how to address the combinations and variations of compliance auditing within the structure of the ISSAI 4000 series and how to express the contents related to these issues, both in the sense of volume and the authority attached to the documents.

The main issue for the committee to consider is what would be the authority attached to documents in the ISSAI 4000 series expressing the specific issues: Would they contain additional requirements for auditors or would they add on to the guidance provided in the common authoritative standard?

One concrete example of the issue of the authority of documents on specific issues may be the document expressing how compliance auditing is performed related to the audit of financial statements. This document would contain all cross-references to the ISSAI 1000 series presently in ISSAI 4200. Whether to give an additional document of this kind an authoritative status or not would lead to considerations of whether or not all requirements of the ISSAI 1000 series is to be followed when performing compliance audits related to the audit of financial statements.

Another example are the concepts and additional needs of courts performing compliance audit. Would they impose additional requirements on the audit process?

Comments of the chair

In view of the experiences of implementing the ISSAI 4000 series, we have noticed that there is a certain learning ladder for many SAIs in order to be able to comply with the ISSAI 4000 series. Hence, in light of the ambition set for SAIs in complying with the ISSAIs, we would consider it reasonable for the ISSAI 4000 series to only contain requirements in a common authoritative standard. Hence, additional documents should in our opinion only provide guidance. Yet we do acknowledge arguments in favor of the documents covering specific issues also containing requirements and receiving the authority of a standard as there might be reasonable arguments for further need of requirements.

As concerns which are there is a need to develop documents on specific issues, the previous work of the committee would imply one document on compliance auditing performed related to the audit of financial statements and one document on compliance auditing performed in the context of courts of



accounts. Furthermore, the chair suggests other needs for documents on specific issues to be identified through the process of contents development.

4. Priorities regarding contents development

The need for further maintenance of the ISSAI 4000 series was identified by CAS already at the meeting in Stockholm in 2009, where a number of issues not yet considered finally developed in the Compliance Audit Guidelines sent for endorsement were identified as maintenance issues. These issues were:

- Materiality/pervasiveness
- Sampling
- Limited vs. reasonable assurance
- Need for application material
- Opinion – positive vs negative report
- How to set up a monitoring system

Committee members have already reflected upon these issues in maintenance papers presented at the CAS meeting in Vilnius in 2012.

During the harmonization project the terminology, audit approaches and standard setting solutions developed by CAS have been merged and challenged by the other audit types into a common platform for public sector auditing. The main substance and concepts brought in by CAS have been preserved in the final documents. This has shown the professional strength of CAS' products and also identified areas in need of further development in the Compliance Audit Guidelines. The main areas in need of development are the following:

1. The audit process leading to a compliance audit opinion
ISSAI 4200 gives the option of giving a compliance audit opinion. Still, the audit process described in the standard does not differ significantly from ISSAI 4100. There is a need to explore further how to design at an ISSAI level the audit process leading to a compliance audit opinion. This would also include the process leading to a positive vs. negative report already identified as a maintenance issue.
2. Identifying the subject matter and criteria
In direct reporting engagements it is the auditor who evaluates the subject matter against criteria, and it is often also the auditor who identifies the subject matter and criteria. Subject matter and criteria have their own sections in the Compliance Audit Guidelines, yet the process of identifying them may be considered a sub-audit process in itself. Hence, the maintenance of the ISSAI 4000 series should explore the needs for portraying the process of identifying the subject matter and criteria in direct reporting engagements.
3. How to achieve assurance



Compliance audits in accordance with the ISSAIs are performed by obtaining assurance.⁶ This assurance is to be obtained in line with the definitions of assurance in public sector auditing developed in the new ISSAI 100.⁷ In compliance auditing assurance is provided both as reasonable and limited assurance and both in direct reporting and attestation engagements, in addressing subject matters of both quantitative and qualitative nature. How this assurance is obtained at a concrete level is yet to be explored at guidance level in the ISSAI 4000 series. This would also include sampling, already identified as a maintenance issue.

4. Authorities and propriety

In CAS' products two basic concepts have been developed specifically for compliance audits in the public sector, which are *authorities* and *propriety*. These concepts are now accepted and identified at a conceptual level, but they are yet to be elaborated and rendered concrete as requirements and guidance to the auditor in the audit process.

Furtheron, during the harmonization project terminology and requirements in ISSAI 400 has been adjusted to updated audit terminology and harmonized with the other audit types. This has also led to the following changes that need to be included in the maintenance of the ISSAI 4000 series:

- Legal basis is deleted as a concept and is being replaced with the elements of compliance auditing.
- Professional judgement and skepticism is a new principle
- Audit team management and skills is a new principle
- Audit scope is a new principle
- Control environment is added to the principle of internal controls
- Audit risk is separated from risk assessment

All these issues are in need of elaboration in the maintenance of the ISSAI 4000 series.

Comments of the chair

The maintenance process of the ISSAI 4000 series is well prepared through CAS discussions starting in 2009, and maintenance issues identified at an early stage have shown to become more relevant as the ISSAI 4000 series is being implemented and the ISSAI 400 developed. Considering the maintenance needs identified in 2009, only the need for application material is not still a CAS priority, since this is thoroughly covered through implementation programmes of the ISSAIs.

Hence, the priorities of the chair regarding the contents development during the maintenance of the ISSAI 4000 series in the strategic period of 2013–2014 are the following:

1. The audit process leading to a compliance audit opinion
2. Identifying the subject matter and criteria
3. How to achieve assurance
4. Authorities and propriety
5. Updating requirements, audit process and concepts in the following areas:
 - Materiality
 - Elements
 - Professional judgement and skepticism

⁶ ISSAI 400 paragraphs 40 and 41, ISSAI 4100/4200 section 2.2.

⁷ ISSAI 100 paragraphs 31, 32 and 33



- Audit team management and skills
- Audit scope
- Control environment
- Audit risk/risk assessment

The chair suggests the committee establishes four maintenance groups to deal with the issues 1-4 on the list of priorities in order to present proposals on further development of the issue at the CAS meeting in 2014. The issues listed on item 5 will be handled by the secretariat and presented before the committee at the next meeting.

5. Issues for consideration

The chair would like the committee to address the following issues related to maintenance:

1. Would the further maintenance of the ISSAI 4000 series start with a restructuring of the documents where one common authoritative standard comprises the main requirements on compliance auditing?
2. What would be the appropriate number of requirements and volume of guidance in such a standard?
3. Would documents containing the specific issues in compliance audit contain further requirements than the common authoritative standard or additional guidance material?
4. What documents would be most needed as additional guidance or standards to a common authoritative standard on compliance auditing?
5. Are the suggested priorities regarding contents development during maintenance appropriate?



Appendix 1:
CAS maintenance strategy 2013–2016
Illustrative example of the number of requirements and volume of guidance
in an authoritative standard on compliance auditing

Case: Suitable criteria

Requirement: Auditors shall identify suitable criteria.⁸

The auditor should identify suitable criteria to provide a basis for evaluating the audit evidence and developing audit findings and conclusions. The criteria should be made available to the intended users and others as appropriate. They should also be communicated to the responsible party.

Guidance: Criteria⁹

1. The criteria, or the benchmarks against which the subject matter will be compared, must also be identified. In performing compliance audits, the identification of the criteria is an essential step in the audit planning process. Some examples of criteria in relation to compliance auditing are set out in Appendix 1 and 1-A.
2. Criteria may be formal, such as a law or regulation, ministerial directive or the terms of a contract or agreement. Criteria may also be less formal such as a code of conduct or principles of propriety, or they may relate to expectations regarding behaviour, for example what may be considered acceptable in regard to class of travel or levels of hospitality and entertainment at government expense if such limits are not explicitly stated elsewhere. Administrative guidelines used as criteria should be in compliance with laws and regulations. The sources used as a basis for the audit criteria can in itself be part of the compliance audit.
3. The criteria should be suitable. This means that the criteria should have the following characteristics:
 - a) **Relevant** – relevant criteria provide meaningful contributions to the information and decision making needs of the intended users of the audit report
 - b) **Reliable** – reliable criteria result in reasonably consistent conclusions when used by another auditor in the same circumstances
 - c) **Complete** – complete criteria are those that are sufficient for the audit purpose and do not omit relevant factors. They are meaningful and make it possible to

⁸ Source: ISSAI 400 Endorsement version

⁹ Source ISSAI 4100/ISSAI 4200 chapter 6.3



provide the intended users with a practical overview for their information and decision making needs.

- d) **Objective** – objective criteria are neutral and free from any bias on the part of the auditor or on the part of management of the audited entity. This means that criteria cannot be so informal such that assessment of the subject matter information against the criteria would be very subjective, and may lead other public sector auditors to reach a very different conclusion.
 - e) **Understandable** – understandable criteria are those that are clearly stated, contribute to clear conclusions and that are comprehensible to the intended users. They are not subject to wide variations in interpretation.
 - f) **Comparable** - comparable criteria are consistent with those used in similar audits of other similar agencies or activities, and with those used in previous audits of the entity
 - g) **Acceptable** - acceptable criteria are those to which independent experts in the field, audited entities, the legislature, the media and the general public are generally agreeable
 - h) **Available** – criteria should be made available to intended users such that they understand the nature of the audit work performed and the basis for the audit report
4. Criteria include matters that may have a significant impact on the objective of a particular audit. Therefore, in performing compliance audit, public sector auditors determine that the criteria are suitable and relevant to the subject matter and the objectives of the particular audit being performed. Once suitable criteria have been identified based on the characteristics set out above, they then must be appropriately 'operationalised' for the particular circumstances of each audit so as to be able to reach meaningful audit conclusions.
 5. The determination of criteria can be straight forward, but in some cases the identification may be more complex. In some cases public sector auditors may find checklists a helpful means in gaining an overview of the suitable criteria to be used. Public sector auditors use a number of sources to assist in the identification of criteria. Some examples of such sources are set out in Appendix 2.
 6. In many compliance audits, the applicable criteria will be clearly identifiable. This may be the case where a clear and uncomplicated law or regulation forms the criteria. The documented intentions or premises for resolutions of the legislature may also assist the auditor in identifying the appropriate criteria.
 7. If situations arise where there may be doubt as to what is the correct interpretation of the relevant law, regulation or authority, public sector auditors 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 auditors may also consider relevant earlier decisions made by judicial authorities.

8. However, when propriety is the subject matter of the compliance audit, the criteria may become more difficult to identify as it may be less formal and may include public expectations in regard to the actions and behaviour of public officials. In these cases, public sector auditors must be more thorough in their work to identify suitable criteria. The need to identify suitable criteria does not preclude public sector auditors from reporting identified breaches of what may be considered acceptable behaviour by public officials, if circumstances so warrant.
9. In the process of identifying suitable criteria, public sector auditors consider materiality related to the risk of potential non-compliance for each topic subject to audit (budgetary law, other specific laws, terms of a contract etc, as well as propriety where relevant). Materiality considerations include both quantitative aspects (size) and qualitative aspects (nature and characteristics).
10. Public sector auditors ensure that the criteria to be used adequately reflect the topic subject to audit in its entirety. In rare cases, where the audit may be of limited scope and may only cover certain parts of a law or regulation, this limited scope should be clearly stated in the auditor's report. If public sector auditors make use of guidelines, checklists or other material provided by the audited entity or other administrative authorities for the purpose of identifying the suitable audit criteria, they must take due care in assuring through appropriate audit procedures that the material used adequately reflects the applicable law, regulation, etc.
11. In some cases, provisions of relevant legislation may be unclear, for example where an act of legislation provides that more specific provisions should be set out by the relevant administrative body and these provisions have not yet been developed. In such cases, public sector auditors clearly state in the audit report what they believe the relevant legislation requires, or that the scope of the audit has been limited and the reasons for this limitation. For example, the report may state that insufficient clarity of law has limited the audit criteria applied and that there is a need for remedial measures to be taken.
12. In some rare cases, the criteria may be conflicting, for example when there is a conflict between different sources of law and the issue has not been solved by the relevant administrative or judicial authorities. In such cases it is very important to understand the intentions behind the particular criteria and to identify any consequences arising from such conflict. It may also be necessary to elaborate on instances of conflicting criteria in the auditor's report such that remedial measures may be taken by the appropriate bodies.



13. Approaches to help identify suitable criteria in these types of dilemmas may include:
 - a) Applying a 'theoretical' approach, by allowing experts in the field to answer questions such as: 'what ought to be the ideal results under perfect conditions according to rational thinking or best-known comparable practice?' or
 - b) Defining and obtaining support for well-founded and realistic criteria by applying an 'empirical' approach involving discussions with stakeholders and decision makers
14. The audit approach may also be broken down into parts, or the scope narrowed, such that clearly identifiable criteria may be applied.
15. Notwithstanding the above, the criteria should be made available to the intended users and others as appropriate, for example by including the criteria in the auditor's report, or making reference to the criteria if they are readily available in another format.
16. In situations where the audit criteria are, for whatever reason, not considered suitable, the SAI may encourage the appropriate bodies to formulate clearly the general principles to be followed in public sector entities for such matters.



**Appendix 2:
Draft table of contents of a possible ISSAI 4000
Compliance Audit Standard of INTOSAI**

INTRODUCTION

AUTHORITY OF THE STANDARD

DEFINITIONS

THE ELEMENTS AND THEIR RELATION TO THE AUDIT PROCESS

Authorities and criteria

Subject matter

The three parties in compliance auditing

Assurance in compliance auditing

THE AUDIT PROCESS

General requirements

Professional judgment and skepticism

Quality control

Audit team management and skills

Audit risk

Materiality

Documentation

Communication

Requirements related to the audit process

Planning and designing a compliance audit

- Audit scope
- Subject matter and criteria
- Understanding the entity
- Understanding internal controls and control environment
- Risk assessment
- Risk of fraud
- Audit strategy and audit plan

Audit evidence

Evaluating audit evidence and forming conclusions

Reporting

Follow-up