

Discussion paper on audit conclusions and opinions in compliance auditing

Purpose and structure

1. The CAS maintenance group # 2 is responsible for further developing on the issue of assurance and the audit process leading to a compliance audit opinion. The group's mandate mentioned possible questions to address regarding assurance and audit opinions/conclusions.
2. This paper will tackle the questions for audit opinions/conclusions, namely:
 - a. Is an opinion only relevant in attestation engagements?
 - b. Is an opinion only given in relation to the financial statements?
 - c. Can an opinion only be given on quantitative subject matters?
 - d. Do the existing cross-references to the ISSAI 1000-series cover the need for requirements and guidance in order to give a compliance audit opinion?
3. Annex I cites all relevant stipulations of ISSAI 100, 400 and 4200 on audit conclusions and opinions, which have been the starting point for the discussions contained in this paper.
4. Any changes to current standards in substance may require thorough reflections, discussions and careful and extensive explanations.

Introduction

5. Compliance auditing may cover a wide range of subject matters, and can be performed to provide either reasonable or limited assurance, using several types of criteria, evidence gathering procedures and reporting formats.
6. Auditors should prepare a report based on the principles of completeness, objectivity, timeliness and a contradictory process. The forms of reporting may be defined in law or by the mandate of the SAI. Nonetheless, the audit report normally contains a section presenting the outcome or result of the audit work. This may be presented and expressed in various ways:
 - i) as a single statement of opinion on compliance written in a clear and standard manner or

- ii) as a conclusive section laying down the results, outcome and/or impact of the audit results in non-standardised manner or
- iii) as a more elaborate answer to specific audit questions or
- iv) A description of the findings based on the audit work performed.

The audit work as presented in the audit scope shall be the basis for the opinion, conclusion or other presentation of the audit results. Reference to the audit scope and reiteration thereof should be made in this section of the auditor's report.

What is the difference between audit conclusions and audit opinions?

7. ISSAI 4200 provides definitions of an audit opinion and audit conclusion. The concept of an audit conclusion is broader, and encompasses the concept of an audit opinion.
8. ISSAI 400 stipulates that delivering an audit opinion would normally require a more elaborate audit strategy and approach. The concept of "elaborate" is not sufficiently defined. ISSAIs should be more specific and state, for example, how the assurance should be obtained (e.g. use of audit risk model, systems testing, substantive testing), how sampling if needed should be performed by way of delivering of some examples. It should be discussed if a more elaborate audit strategy and approach is to be understood as leading to reasonable assurance.
9. ISSAI 100 requires audit conclusions and opinions explicitly convey the level of assurance, and this applies equally to all attestation engagements and certain direct reporting engagement. It allows for some direct reporting engagement to provide the necessary degree of confidence by explicitly explaining how findings, criteria and conclusions were developed, and how they result in a certain overall conclusion. It should be clarified if all compliance audits' opinions/conclusions should convey the level of assurance and, if not, why only some should.
10. Issues which also are important factors in the discussion of difference are such as variance in findings, precision of audit results, audit scope and depth. Thus, audit opinion would have a narrower confidence level in comparison to other types of audit conclusions. It should be discussed which requirements conclusions should fulfil.

Is an opinion only relevant in attestation engagements?

11. There are two types of assurance audits:
 - a. In attestation engagements, the auditee assesses itself the subject matter against the criteria, and presents the subject matter information, independently from the auditor. Based on this, the auditor issues a conclusion as to whether the subject matter information is, in all material respects, free from misstatement or error and/or whether the subject matter complies, in all material respects, with the established criteria. Generally, financial audits are attestation engagements.
 - b. In direct reporting, it is the auditor who selects the subject matter and criteria taking into consideration risk and materiality, and then assesses it against the criteria. The results are presented in the form of findings, conclusions, recommendations or an opinion. Performance audits are examples of direct reporting.
12. In ISSAI 400 it is laid down that compliance auditing may be attestation or direct reporting engagements, or both at once. It is worth discussing under what circumstances the compliance auditing might be both types of engagement at the same time given that one of the differencing factors is the auditors' independence from the preparation of subject matter information.
13. An audit opinion is common in attestation engagements, whereas the answering of specific audit questions is more often used in direct reporting engagements. Additionally, it states that conclusions may be expressed in various ways: as a single clear written statement of opinion on compliance or as a more elaborate answer to specific audit questions (see also paragraph 6)
14. In principle it should be possible to provide an opinion (or conclusion) for both direct reporting and attestation engagements. In both cases, for compliance audits the audit opinion or conclusion should provide explicitly the level of assurance. An audit opinion should be in a standardised format.
15. In direct reporting engagements, other forms of audit conclusions could also be used e.g. more elaborate answers to specific audit questions.

Is an opinion only given in relation to the financial statements?

16. The ISSAI 1000 series include several standards dealing with an audit opinion, but audit opinions are not reserved for the financial statements' audits. ISSAI 4200 has for a number of years clearly stated that if the compliance audit is performed together with the financial statements' audit, the conclusion thereon may take the form of an audit opinion.
17. The more recent ISSAI 400 sees this relation slightly from a different perspective. It states that an audit 'conclusion may take the form of a clear written statement of opinion on compliance, often in addition to the opinion on the financial statements'. This expands on the scope for using audit opinions concerning compliance audits. Audit opinions can be used for compliance audits performed together with financial audits and can also be also used for standalone compliance audits.
18. In both cases, the requirements for issuing of an audit opinion are the same, and require more elaborate audit strategy, -approach and evidence base along with a high level of assurance.
19. While the provision of an audit opinion entails more requirements, it also gives more precision and focus on problematic parts or areas of non-compliance – where relevant.

Can an opinion only be given on quantitative subject matters?

20. Some subject matters are qualitative and more subjective in nature (e.g. compliance to procedural requirements or behaviour). In general, qualitative subject matters are not as easy to measure as quantitative subject matters. This may prove to be problematic in the discussion of ensuring sufficient and appropriate audit evidence and ultimately assurance to support an audit opinion. Assessing audit evidence for qualitative subject matter may require auditors to exercise professional judgment to a larger extent as compared to quantitative subject matter.
21. ISSAI 4200 requires that the subject matter should be of such a nature that it is possible to gather evidence to support reporting in the form of a reasonable assurance opinion. It seems possible that it could be achieved for both the qualitative and quantitative subject matter if they are identifiable and it is possible to assess them against suitable criteria.

22. For qualitative subject matters, practical implications of obtaining sufficient audit evidence and more extensive use of professional judgment may lead to higher audit risk. This might reduce the level of assurance the auditor is able to obtain, which would impact on the type of an audit conclusion the auditor may want to or is able to subsequently issue.

Do the existing cross-references to the ISSAI 1000-series cover the need for requirements and guidance in order to give a compliance audit opinion?

23. ISSAI 1000-series cover the financial statements' audits. Indeed many of the concepts covered by them are also relevant for compliance audits. But cross-referencing to the ISSAI 1000-series is likely to lead to confusion between the two concepts, and therefore should be limited. If necessary, it is better to use the relevant passages or text from the ISSAI 1000-series in so far as the agreement between INTOSAI and IFAC permits.

Conclusions

24. The concepts of an audit opinion and conclusion should be kept as set out in ISSAI 4000 series. Further ways of reporting the audit results should also be considered at this level (level four) and possibly elaborated upon.

25. It should be possible to provide an audit opinion (or conclusion) for both direct reporting and attestation engagement.

26. An audit opinion or conclusion can be given for both quantifiable and qualitative subject matters where the guidance for qualitative subject matters needs a lot more development.

27. Audit opinions are not reserved to the financial statements' audits only.

28. Cross-referencing to the ISSAI 1000-series should be limited.

ANNEX I

ISSAI 100

29. There are two types of engagement:

In attestation engagements 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 expressing a conclusion.

In direct reporting engagements it is the auditor who measures or evaluates the subject matter against the criteria. The auditor selects the subject matter and criteria, taking into consideration risk and materiality. The outcome of measuring the subject matter against the criteria is presented in the audit report in the form of findings, conclusions, recommendations or an opinion. The audit of the subject matter may also provide new information, analyses or insights.

32. Depending on the audit and the users' needs, assurance can be communicated in two ways:

Through opinions and conclusions which explicitly convey the level of assurance. This applies to all attestation engagements and certain direct reporting engagements.

In other forms. In some direct reporting engagements the auditor does not give an explicit statement of assurance on the subject matter. In such cases the auditor provides the users with the necessary degree of confidence by explicitly 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.

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Opinion

When an audit opinion is used to convey the level of assurance, the opinion should be in a standardised format. The opinion may be unmodified or modified. An unmodified opinion is used when either limited or reasonable assurance has been obtained. A modified opinion may be:

Qualified (except for) – where the auditor disagrees with, or is unable to obtain sufficient and appropriate audit evidence about, certain items in the subject matter which are, or could be, material but not pervasive;

Adverse – where the auditor, having obtained sufficient and appropriate audit evidence, concludes that deviations or misstatements, whether individually or in the aggregate, are both material and pervasive;

Disclaimed – where the auditor is unable to obtain sufficient and appropriate audit evidence due to an uncertainty or scope limitation which is both material and pervasive. Where the opinion is modified the reasons should be put in perspective by clearly explaining, with reference to the applicable criteria, the nature and extent of the modification. Depending on the type of audit, recommendations for corrective action and any contributing internal control deficiencies may also be included in the report.

ISSAI 400

13. The objective of public-sector compliance auditing, therefore, is to enable the SAI to assess whether the activities of public-sector entities are in accordance with the authorities governing those entities. This involves reporting on the degree to which the audited entity complies with established criteria. Reporting may vary between brief standardised opinions and various forms of conclusions, presented in short or long form. Compliance auditing may be concerned with *regularity* (adherence to formal criteria such as relevant laws, regulations and agreements) 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 auditing, propriety may also be pertinent given the public-sector context, in which there are certain expectations concerning financial management and the conduct of officials. Depending on the mandate of the SAI, the audit scope may therefore include aspects of propriety.

15. Compliance auditing may cover a wide range of subject matter and can be performed to provide either reasonable or limited assurance, using several types of criteria, evidence gathering procedures and reporting formats. Compliance audits may be attestation or direct reporting engagements, or both at once. The audit report may be either long- or short-form, and conclusions may be expressed in various ways: as a single clear written statement of opinion on compliance or as a more elaborate answer to specific audit questions.

34. The subject matter depends on the mandate of the SAI, the relevant authorities and the scope of the audit. Hence the content and scope of compliance audit subject matter can vary widely. The subject matter of an audit may be either general or specific. Some

types of subject matter are quantitative and, often, easily measured (for example payments which do not satisfy certain conditions), while others are qualitative and more subjective in nature (for example behaviour or adherence to procedural requirements).

59. Auditors should prepare a report based on the principles of completeness, objectivity, timeliness and a contradictory process.

The principle of completeness requires the auditor to consider all relevant audit evidence before issuing a report. The principle of objectivity requires the auditor to apply professional judgement and scepticism in order to ensure that all reports are factually correct and that findings or conclusions are presented in a relevant and balanced manner. The principle of timeliness implies preparing the report in due time. The principle of a contradictory process implies checking the accuracy of facts with the audited entity and incorporating responses from responsible officials as appropriate. In both form and content, a compliance audit report should conform to all these principles.

The forms of reporting may be defined in law or by the mandate of the SAI. Nonetheless, the audit report normally contains a conclusion based on the audit work performed. The report may also provide constructive and practical recommendations for improvement where appropriate.

In an attestation engagement the report is generally referred to as the Auditor's Report. Reporting may vary between brief standardised opinions and various forms of conclusions, presented in short or long form. However it appears, the report should be complete, accurate, objective, convincing and as clear and concise as the subject matter permits. Any limitations in the audit scope should be described. The report should clearly state the relevance of the criteria used and the level of assurance provided.

The conclusion may take the form of a clear written statement of opinion on compliance, often in addition to the opinion on the financial statements. It may also be expressed as a more elaborate answer to specific audit questions. While an opinion is common in attestation engagements, the answering of specific audit questions is more often used in direct reporting engagements. Where an opinion is provided the auditor should state whether it is unmodified or has been modified on the basis of the evaluation of materiality and pervasiveness. Delivering an opinion would normally require a more elaborate audit strategy and approach.

31. Definitions

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5. Conclusion – The auditor's report on compliance subject matters normally contains a conclusion based on the audit work performed. When compliance audit is performed together with the audit of financial statements, the conclusion may take the form of an opinion (see Opinion). The conclusion may also be expressed as a more elaborated answer to specific audit questions.

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7. Opinion – The auditor's report on the financial statements may contain a clear written expression of opinion on compliance in addition to the opinion on the financial statements. An unqualified opinion may be expressed when the auditor concludes that, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.

43. Subject matters take many forms and have many different characteristics. Subject matters may be general or very specific in nature. Some are quantitative and can often be easily measured (for example financial performance or condition), while others are qualitative and more subjective in nature (for example behaviour). Nonetheless, the subject matter should be identifiable and it should be possible to assess the subject matter against suitable criteria. Furthermore, the subject matter should be of a nature such that it is possible to gather evidence about the subject matter information sufficient to support reporting in the form of a reasonable assurance opinion.