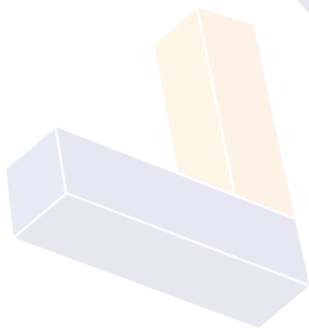


ADVANCED AUDIT AND ASSURANCE

CORPORATE LEVEL

TUTE 11

11.1 – ASSURANCE ENGAGEMENTS



by

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likelihood that the information will meet the needs of an intended user. In this regard, the level of assurance provided by the professional accountant's conclusion conveys the degree of confidence that the intended user may place on the credibility of the subject matter.

Objectives of Assurance Engagement

The objective of the Assurance Engagement is to provide an assurance to the intended users of the information. It can be divided into two aspects

- a) Reasonable Assurance Engagement
- b) Limited Assurance Engagement

Important

When a practitioner undertakes an assurance engagement, it must be clearly understood from the outset whether it is a reasonable assurance engagement or a limited assurance engagement because this will affect the work that the practitioner carries out.

Reasonable Assurance Engagement

Reasonable Assurance is a fairly high level of assurance, but it is not absolute (100%) assurance. With reasonable assurance, the practitioner reduces the risk of expressing an incorrect opinion to an acceptably low level. By reducing the risk of an incorrect opinion to such a low level, the practitioner is able to express his/her opinion in a positive form. In order to give reasonable assurance, a significant amount of testing and evaluation is required to perform by the practitioner. (Eg. Practitioner engage to perform annual statutory audit.

Reasonable Assurance Engagement is an assurance engagement in which the practitioner reduces engagement risk to an acceptably low level in the circumstances of the engagement as the basis for the practitioner's conclusion. The practitioner's conclusion is expressed in a form that conveys the practitioner's opinion on the outcome of the measurement or evaluation of the underlying subject matter against criteria.

Limited Assurance Engagement

Limited Assurance is a lower level of assurance (Moderate Assurance) than reasonable assurance. It allows for a lesser amount of testing and evaluations. As a result, there is a greater risk that the auditor gives an incorrect opinion. Since the risk of an incorrect opinion is higher in a Limited assurance engagement, the practitioner expresses his opinion in a negative form.

The objective of a limited assurance engagement is to reduce assurance engagement risk in a line that is acceptable in the circumstances of the engagement, but where the risk is greater than for reasonable assurance engagements. Limited assurance engagements are not required to relate to financial reports or accounting figures. They may relate to non-financial information, system, controls and practices.

The difference between Reasonable Assurance Engagements and Limited Assurance Engagements

Reasonable Assurance Engagements	Limited Assurance Engagements
The practitioner gathers sufficient and appropriate evidences to be able to draw reasonable assurance.	The practitioner gathers sufficient and appropriate evidences to be able to draw limited assurance.
Gives a positively worded Assurance Opinion	Gives a negatively worded Assurance Opinion
Gives a high level of assurance	Gives a moderate level/low level of assurance
Performs very thorough procedures to obtain sufficient and appropriate evidence, including Test of Controls and Substantive Procedures	Performs fewer procedures – mainly, enquiries and analytical procedures

The confidence level of a reasonable assurance report is higher than the confidence level of a limited assurance report. Therefore, there are more regulations and standards applicable to a reasonable assurance assignment. Also, the procedures carried out will be more thorough and the evidence gathered will need to be of a high quality

REASONABLE ASSURANCE ENGAGEMENTS	
Annual Statutory / External Audit	Annual external audit gives the reader reasonable assurance on the truth and fairness of the financial statements. Auditor's Report does not guarantee that the financial statements are correct, but that they are true and fair within reasonable level.
LIMITED ASSURANCE ENGAGEMENTS	
Prospective Financial Statements	An assurance practitioner may be asked to report on financial forecast that has been prepared by a company. It is not possible to perform a reasonable assurance on information about the future. So, it will I provide limited assurance.
Internal Controls	A limited assurance engagement may report on information prepared by the company about its internal controls or internal control system
Historical Financial Statements	Audit of Interim Financial Statements

A) Elements of Assurance Engagements

- a) Existence of **THREE-PARTY RELATIONSHIP** which involves:
- 1) The Intended Users
 - 2) The Responsible Party
 - 3) The Practitioner

b) SUBJECT MATTER

This is the data to be verified which has been prepared by the responsible party. It can take many forms including financial performance (eg historical financial information), non-financial performance (eg key performance indicators), processes (eg internal control) and behaviour (eg compliance with laws and regulations).

A subject matter may take a variety of forms. A clear understanding of the subject matter is essential when the practitioner performs an assurance engagement. This includes understanding why the users are interested in the subject matter and their relationship to it. Such an understanding affects whether the subject matter of the engagement is appropriate for the purpose and whether the users would understand the assurance conclusion in an appropriate context. Therefore, the practitioner considers whether the subject matter has been defined appropriately and whether the approach to be taken is suitable when accepting an engagement.

The practitioner will consider whether he or she possesses the relevant skills and competences before agreeing to undertake an assurance engagement on the subject matter. Subject matters have different characteristics, including the degree to which information about them is qualitative versus quantitative, objective versus subjective, historical versus prospective and whether it relates to a point in time or covers a period. When undertaking an assurance engagement, therefore, the practitioner considers whether the subject matter is identifiable and capable of being consistently evaluated or measured against criteria; and the availability and the persuasiveness of evidence.

c) CRITERIA

The criteria is the measurement based on which the subject matter is evaluated in order to reach an opinion. These criteria will depend on the nature of the subject matter. Following characteristics should be there.

- 1) **Relevance** – Relevant criteria contribute to conclusions that assist decision making by the intended users
- 2) **Completeness** - Criteria are sufficiently complete when relevant factors that could affect the conclusions in the context of the engagement circumstances are not omitted. Complete criteria include, where relevant, benchmarks for presentation and disclosure, or where it supports the fair description of systems and controls in operation.

- 3) **Reliability** - Reliable criteria allow reasonably consistent evaluation or measurement of the subject matter including, where relevant, presentation and disclosure, when used in similar circumstances by similarly qualified practitioners.
 - 4) **Neutrality** - Neutral criteria contribute to conclusions that are Free from bias.
 - 5) **Understandability** - Understandable criteria contribute to conclusions that are clear, comprehensive, and not subject to significantly different interpretations.
- d) Sufficient appropriate **EVIDENCE** collected as a result of examination
Sufficient and appropriate evidence needs to be gathered to support the opinion on the subject matter.
 - e) Expression of opinion in the form of a **WRITTEN REPORT** issued by the practitioner providing assurance of:
Higher degree as under reasonable assurance engagements
Moderate degree as under limited assurance engagements.

Key Aspects and Requirements when accepting and Managing Assurance Engagements.

Step 01) Ethical and Quality Control Requirements

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Step 02) Engagement Acceptance and Continuance

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Step 03) Planning and Performing Engagement

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Step 04) Assessing the appropriateness of the subject matter

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Step 05) Assessing the suitability of the Criteria

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Step 06) Materiality and Assurance Engagement Risk

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Step 07) Obtaining Evidence & Documentation

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Step 08) Preparation of Assurance Report

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Audit of Financial Statements

“Auditing is an independent examination, conducted by an independent party to ascertain whether the Financial Statements of the Business Organization is prepared in accordance with Sri Lanka Accounting Standards/Applicable Reporting Framework and to ascertain whether those financial statements gives a True and Fair View”

The overall objectives of a Financial audit

To obtain reasonable assurance about whether the financial statement as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditors to express an opinion on whether the financial statement are prepared, in all material respects, in accordance with an applicable financial reporting framework.

Key Elements of the Financial Statement Audit

Tri -Party Relationship	
Subject Matter	
Criteria	
Audit Evidence	
Assurance Report	

Upon completion of the Audit, the Auditor will provide a Reasonable Level of Assurance/ High Level of Assurance

Why the Auditor unable to provide an Absolute Assurance upon completion of the Audit Engagement?

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Review of Financial Statements - (SLSRE 2400)

A limited assurance engagement involves the use of primarily inquiry and analytical procedures to obtain sufficient appropriate evidence.

Although inquiry and analytical procedures are the main sources of evidence, if the practitioner becomes aware of something that makes them think there may be a material misstatement, then further procedures may be necessary (such as substantive procedures). Many of the requirements of the SLSRE are similar to the requirements of an audit. Only relevant requirements must be complied with, but if a requirement is relevant then it must be complied with.

A) Considerations from the Ethical Requirement Perspective

- ✚ The practitioner shall comply with relevant ethical requirements, including those pertaining to independence.
- ✚ The practitioner shall plan and perform the engagement with professional recognizing that circumstances may exist that cause the financial statements to be materially misstated.
- ✚ The practitioner shall exercise professional judgment in conducting a review engagement.

B) Consideration from Quality Control Perspective

- ✚ The engagement partner is competent in assurance and financial reporting.
- ✚ The engagement partner is responsible for the engagement overall.
- ✚ The engagement partner must remain alert for ethical issues during the course of the engagement.
- ✚ A monitoring process must be in place to ensure that quality controls are sufficient and are working effectively.

C) Agreeing Terms and Conditions

- ✚ The practitioner shall agree the terms of the engagement with management or those charged with governance, as appropriate, prior to performing the engagement.
- ✚ This should be done in an engagement letter or other written form.
- ✚ On recurring engagements, the practitioner assesses whether the terms need to change, or whether the engaging party needs to be reminded of the terms.

D) Communication

SLSRE 2400 includes a requirement to communicate with those charged with governance all matters that are important enough to merit their attention.

E) Performing the engagement

- ✚ The practitioner shall determine materiality for the financial statements as a whole, and apply this materiality in designing the procedures and in evaluating the results obtained from those procedures.
- ✚ Materiality must also be revised as the engagement progresses
- ✚ The practitioner shall obtain an understanding of the entity and its environment, and the applicable financial reporting framework
- ✚ Procedures are then designed to address all material items and to focus on areas where material misstatements are more likely. The main procedures are enquiry and analytical procedures.
- ✚ Procedures should be performed to address any specific issues, such as:
 - ✚ Related parties (remain alert and if they are identified, inquire about them)
 - ✚ Fraud and non-compliance with laws or regulations (if found, communicate and consider effect on conclusion)
 - ✚ Going concern
- ✚ It is a requirement to obtain evidence that the financial statements agree to accounting records.
- ✚ If a material misstatement is discovered then additional procedures are performed to enable a conclusion to be formed.
- ✚ Responsibilities in relation to subsequent events are similar to those on an audit.

F) Written representations

Various written representations are required:

- ✚ To confirm that management has fulfilled its responsibilities as set out in the engagement letter
- ✚ To confirm that management has disclosed various matters to the practitioner, eg the identity of any related parties, facts relating to any frauds

If these are not provided, then discuss the matter with management or those charged with governance, and re-evaluate management's integrity. If management lacks integrity, then the practitioner must disclaim a conclusion.

G) Reporting

There are some important differences between a review report and an auditor's report:

Audit Report	Review Report
Opinion	Conclusion
Reasonable Assurance	Limited Assurance
Positive form of words	Negative form of words

INDEPENDENT PRACTITIONER'S REVIEW REPORT

[Appropriate Addressee]

Report on the Financial Statements⁵

We have reviewed the accompanying financial statements of ABC Company, which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's⁶ Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Sri Lanka Accounting Standard for Small and Medium-sized Entities,⁷ and for such internal control as management

determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Practitioner's Responsibility

Our responsibility is to express a conclusion on the accompanying financial statements. We conducted our review in accordance with Sri Lanka Standard on Review Engagements (SLSRE) 2400 (Revised), *Engagements to Review Historical Financial Statements*. SLSRE 2400 (Revised) requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements.

A review of financial statements in accordance with SLSRE 2400 (Revised) is a limited assurance engagement. The practitioner performs procedures, primarily consisting of making inquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with Sri Lanka Standards on Auditing. Accordingly, we do not express an audit opinion on these financial statements.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that these financial statements do not present fairly, in all material respects, *(or do not give a true and fair view of)* the financial position of ABC Company as at December 31, 20X1, and *(of)* its financial performance and cash flows for the year then ended, in accordance with the Sri Lanka Accounting Standard for Small and Medium-sized Entities.

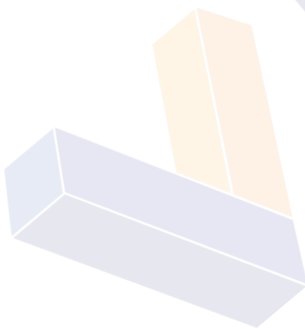
Report on Other Legal and Regulatory Requirements

[Form and content of this section of the practitioner's report will vary depending on the nature of the practitioner's other reporting responsibilities.]

[Practitioner's signature]

[Date of the practitioner's report]

[Practitioner's address]



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Review of Interim Financial Information performed by the independent auditor of the entity – (SLSRE 2410)

This subject is covered by SLSRE 2410 Review of Interim Financial Information Performed by the Independent Auditor of the Entity.

General principles

The auditor should comply with **ethical principles** relevant to the audit when carrying out an interim review and should apply **quality control procedures** applicable to the individual engagement. In addition, the auditor should plan and perform the engagement with an attitude of **professional scepticism**. The auditor should agree the terms of the engagement with the client (these will not be the same terms as for the audit, as the review will result in a lower level of assurance than the annual audit), with a view to providing negative assurance.

The auditor should possess sufficient **understanding of the entity and its environment** to understand the types of misstatement that might arise in interim financial information and to plan the relevant procedures (mainly enquiry and analytical review) to enable them to ensure that the financial information is prepared in accordance with the applicable financial reporting framework.

Factors to consider when perform Review on the Interim Financial Statements

- ✚ Reading last year's audit and previous review files
- ✚ Considering any significant risks that were identified in the prior year audit
- ✚ Reading the most recent and comparable interim financial information
- ✚ Considering materiality
- ✚ Considering the nature of any corrected or uncorrected misstatements in last year's financial statements
- ✚ Considering significant financial accounting and reporting matters of ongoing importance
- ✚ Considering the results of any interim audit work for this year's audit
- ✚ Considering the work of internal audit
- ✚ Asking management what their assessment is of the risk that the interim financial statements might be affected by fraud
- ✚ Asking management whether there have been any significant changes in business activity, and if so, what effect they have had

- ✚ Asking management about any significant changes in internal controls and the potential effect on preparing the interim financial information
- ✚ Asking how the interim financial information has been prepared and the reliability of the underlying accounting records

Procedures to follow

In General

- ✚ Reading the minutes of meetings of shareholders, those charged with governance and other appropriate committees
- ✚ Considering the effect of matters giving rise to a modification of the audit or review report, accounting adjustments or unadjusted misstatements from previous audits
- ✚ If relevant, communicating with other auditors auditing different components of the business
- ✚ Analytical procedures designed to identify relationships and unusual items that may reflect a material misstatement
- ✚ Reading the interim financial information and considering whether anything has come to the auditors' attention indicating that it is not prepared in accordance with the applicable financial reporting framework
- ✚ Agreeing the interim financial information to the underlying accounting records

The auditor should make enquiries of members of management responsible for financial and accounting matters about

- ✚ Whether the interim financial information has been prepared and presented in accordance with the applicable financial reporting framework
- ✚ Whether there have been changes in accounting policies
- ✚ Whether new transactions have required changes in accounting policies
- ✚ Whether there are any known uncorrected misstatements
- ✚ Whether there have been unusual or complex transactions, eg disposal of a business segment
- ✚ Significant assumptions relevant to fair values
- ✚ Whether related party transactions have been accounted for and disclosed correctly
- ✚ Significant changes in commitments and contractual obligations

Report on Review of Interim Financial Information

(Appropriate addressee)

Introduction

We have reviewed the accompanying balance sheet of ABC Entity as of 31 March 20X1 and the related statements of income, changes in equity and cash flows for the three-month period then ended, and a summary of significant accounting policies and other explanatory notes. Management is responsible for the preparation and fair presentation of this interim financial information in accordance with (indicate applicable financial reporting framework). Our responsibility is to express a conclusion on this interim financial information based on our review.

Scope of Review

We conducted our review in accordance with Sri Lanka Standard on Review Engagements 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity'. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Sri Lankan Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim financial information does not give a true and fair view of (or 'does not present fairly, in all material respects,') the financial position of the entity as at 31 March 20X1, and of its financial performance and its cash flows for the three-month period then ended in accordance with (applicable financial reporting framework, including a reference to the jurisdiction or country of origin of the financial reporting framework when the financial reporting framework used is not Sri Lankan Financial Reporting Standards).

AUDITOR

Date

Address