



Assurance Engagements and Related Services

Mr. Nilantha Weerasingha



JMC Jayasekera Management Centre (Pvt) Ltd
Pioneers in Professional Education

65/2A, Chittampalam Gardiner Mawatha, Colombo 02 | T: +94 112 430451 | E: info@jmc.lk | F: +94 115 377917

Assurance Engagements and Related Services

(Think - Do everything you should do. When it ought to be done. Whether you like or not)

01. What is assurance?

Assurance engagement is an engagement performed by a practitioner to enable himself to express an opinion about the measurement of subject matter against a criteria. Practitioner's expression of opinion raise the confidence of the users over the measurement of subject matter subject to the criteria applicable under consideration.

To summarize the above formal definition, read through the following example to understand how assurance engagement is performed and how it enhances the confidence of users.

Example

Management (responsible party) of company A Ltd fulfilled its responsibility of evaluating entity's financial position, financial performance and changes in cash flows (these all three aspects are in short the subject matter) by publishing financial statements in accordance with International Financial Reporting Standards (criteria) and the assets, liabilities etc are recognized, measured, presented and disclosed in the financial statements (subject matter information) as per the requirements of IFRSs.

Practitioner (auditor) is appointed by the shareholders (users) to express his opinion (assurance) in the form of a report over the recognition, measurement, presentation and disclosures i.e. financial statements (subject matter information) made by the management (responsible part) are actually in accordance with IFRSs (criteria) and the actual financial position, performance and changes in cash flow (subject matter).

From the definition of assurance engagement and also from the above example we understood that not every engagement undertaken by the practitioner amounts to assurance engagement. For an engagement to be assurance engagement it must have the following FIVE essentials or elements (also known as essentials or elements of assurance engagements):

1. Existence of three party relationship which involves:
 1. practitioner
 2. a responsible party
 3. intended users
2. Subject matter
3. Criteria;
4. Sufficient appropriate evidence collected as a result of examination
5. Expression of opinion in the form of a written report issued by the practitioner providing assurance of:
 1. Higher degree as under reasonable assurance engagements.
 2. Moderate degree as under limited assurance engagements.

The outcome of the evaluation or measurement of a subject matter is the information that results from applying the criteria to the subject matter. For example:

- The recognition, measurement, presentation and disclosure represented in the financial statements (outcome) result from applying a financial reporting framework for recognition, measurement, presentation and disclosure, such as International Financial Reporting Standards, (criteria) to an entity's financial position, financial performance and cash flows (subject matter).
- An assertion about the effectiveness of internal control (outcome) results from applying a framework for evaluating the effectiveness of internal control, such as COSO4 or CoCo,5 (criteria) to internal control, a process (subject matter).

02. Scope of the Framework

- Not all engagements performed by practitioners are assurance engagements. Other frequently performed engagements that do not meet the above definition (and therefore are not covered by this Framework) include:
 - Engagements covered by International Standards for Related Services, such as agreed-upon procedures engagements and compilations of financial or other information.
 - The preparation of tax returns where no conclusion conveying assurance is expressed.
 - Consulting (or advisory) engagements, such as management and tax consulting.
- The following engagements, which may meet the definition in paragraph 7, need not be performed in accordance with this Framework:
 - Engagements to testify in legal proceedings regarding accounting, auditing, taxation or other matters.

03. Engagement Acceptance

A practitioner accepts an assurance engagement only where the practitioner's preliminary knowledge of the engagement circumstances indicates that:

- (a) Relevant ethical requirements, such as independence and professional competence will be satisfied; and
- (b) The engagement exhibits all of the following characteristics:
 - (i) The subject matter is appropriate;
 - (ii) The criteria to be used are suitable and are available to the intended users;
 - (iii) The practitioner has access to sufficient appropriate evidence to support the practitioner's conclusion;
 - (iv) The practitioner's conclusion, in the form appropriate to either a reasonable assurance engagement or a limited assurance engagement, is to be contained in a written report; and
 - (v) The practitioner is satisfied that there is a rational purpose for the engagement. If there is a significant limitation on the scope of the practitioner's work

04. The key elements of an assurance engagement are as follows:

- Three people or groups of people involved
 - The practitioner (accountant)
 - The intended users
 - The responsible party (the person(s) who prepared the subject matter)
- A subject matter

As we shall see below, the subject matter of an assurance engagement may vary considerably. However, it is likely to fall into one of three categories:

- Data (for example, financial statements or business projections)
- Systems or processes (for example, internal control systems or computer systems)
- Behavior (for example, social and environmental performance or corporate governance)
- Suitable criteria

The person providing the assurance must have something by which to judge whether the information is reliable and can be trusted. So for example, in an assurance engagement relating to financial statements, the criteria might be accounting standards. The practitioner will be able to test whether the financial statements have been put together in accordance with accounting standards, and if they have, then the practitioner can conclude that there is a degree of assurance that they are reliable.

In the context of company behavior, suitable criteria to judge whether something is reliable and can be trusted might be the Combined Code on Corporate Governance, or, if the company has one, its published Code of Practice.

- Sufficient appropriate evidence to support the assurance opinion

The practitioner must substantiate the opinion that he draws in order that the user can have confidence that it is reliable. The practitioner must obtain evidence as to whether the criteria have been met

- A written report in appropriate form

Lastly, it is required that assurance reports are provided to the intended users in a written form and contain certain specified information. This adds to the assurance that the user is being given, as it ensures that key information is being given and that the assurance given is clear and unequivocal.

05. Level of Assurance

The Framework identifies two types of assurance engagement:

- Reasonable assurance engagement
- Limited assurance engagement

The key differences between the two types of assurance engagement are therefore:

- The evidence obtained
- The type of opinion given

Summary of Types Engagement

Type of engagement	Evidence sought	Conclusion given
Reasonable assurance	Sufficient and appropriate	Positive
Limited assurance	Sufficient and appropriate (lower level)	Negative

06. Differences Between Reasonable Assurance Engagements and Limited Assurance Engagements

This Appendix outlines the differences between a reasonable assurance engagement and a limited assurance engagement discussed in the Framework.

Type of engagement	Objective	Evidence-gathering procedures	The assurance report
Reasonable assurance engagement	A reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement, as the basis for a positive form of expression of the practitioner's conclusion	<p>Sufficient appropriate evidence is obtained as part of a systematic engagement process that includes:</p> <ul style="list-style-type: none"> • Obtaining an understanding of the engagement circumstances; • Assessing risk; • Responding to assessed risks; • Performing further procedures using a combination of inspection, observation, confirmation, re-calculation, re-performance, analytical procedures and inquiry. Such further procedures 	Description of the engagement circumstances, and a positive form of expression of the conclusion

		<p>involve substantive procedures, including, where applicable, obtaining corroborating information, and depending on the nature of the subject matter, tests of the operating effectiveness of controls; and</p> <ul style="list-style-type: none"> Evaluating the evidence obtained 	
Limited assurance engagement	A reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement but where that risk is greater than for a reasonable assurance engagement, as the basis for negative form of expression of the practitioner's conclusion.	Sufficient appropriate evidence is obtained as part of a systematic engagement process that includes obtaining an understanding of the subject matter and other engagement circumstances, but in which procedures are deliberately limited relative to a reasonable assurance engagement	Description of the engagement circumstance, and a negative form of expression of the conclusion

07. Audit

Definition

The objective of an audit of financial statements is to enable the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework.

The key criteria of an assurance engagement can be seen in an audit as follows:

- Three party involvement

- The shareholders (users)
- The board of directors (the responsible party)
- The audit firm (the practitioner)
- Subject matter
 - The financial statements
- Relevant criteria
 - Law and accounting standards
- Evidence

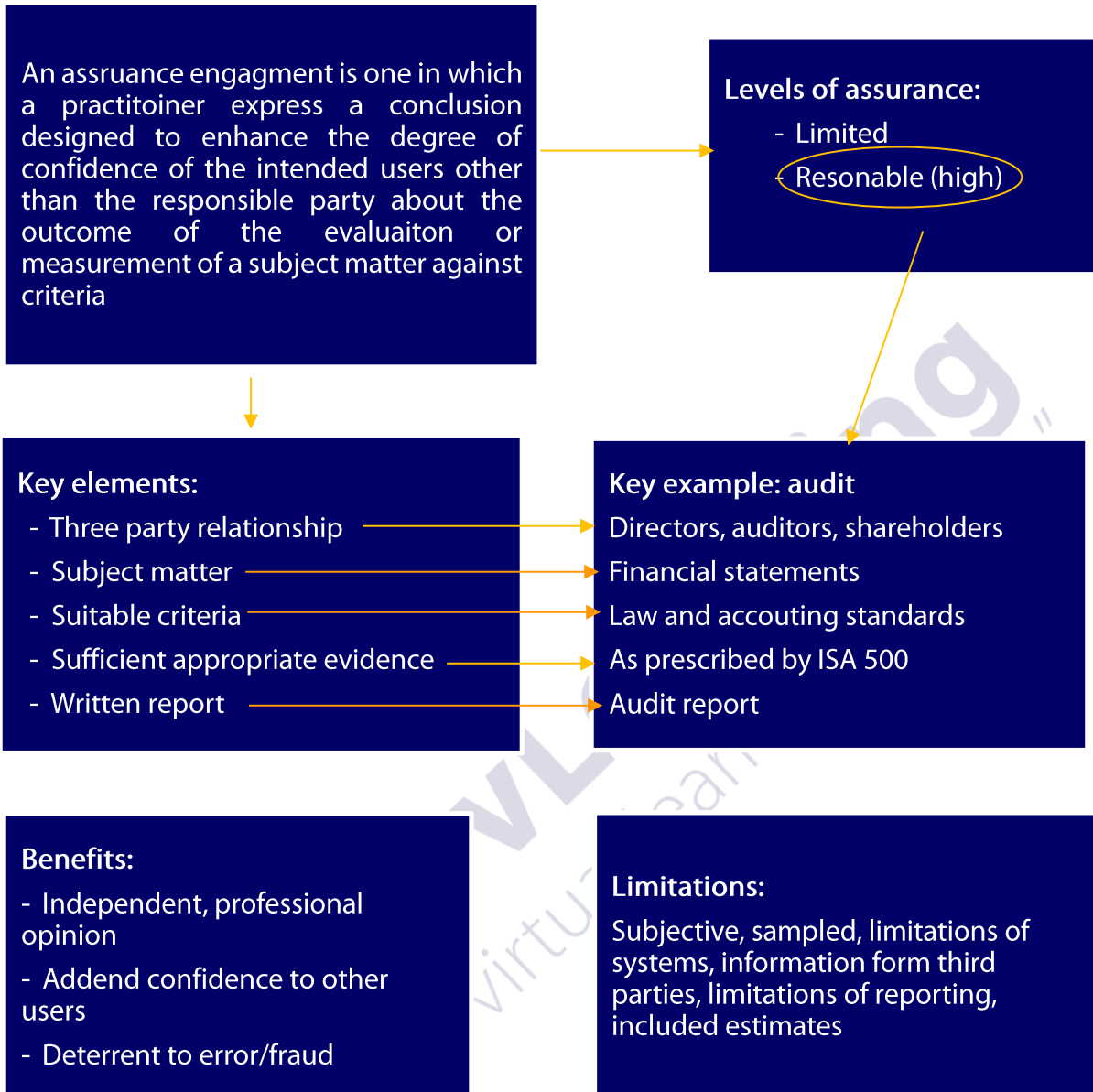
As has been said earlier, sufficient and appropriate evidence is required to support an assurance opinion.
- Written report in a suitable form
 - Again, as has been said, an assurance report is a written report issued in a prescribed form. We will look at the specific requirements for an audit report in Chapter 4.

08. Why can assurance never be absolute?

- Assurance can never be absolute.
- Assurance provision has limitations which may not be understood by users.
- The expectations gap also adds to the lack of guarantee given by assurance.



Summary



Questions

01. Can we provide assurance service on behalf of internal control? If so, Explain 5 element of assurance engagement for an internal control.
02. What is the difference between reasonable assurance & limited assurance?
03. Why is assurance important?
04. Name 4 limitations of an assurance service.

