

PACIFIC ASSOCIATION OF SUPREME AUDIT INSTITUTIONS



*“Pacific Auditors Working
Together”*

REGIONAL COMPLIANCE AUDIT MANUAL

2020

FOREWORD

This manual is the third of PASAI's suite of Regional Audit Manuals. The other components of this suite are the manuals for Financial Audits and Performance Audits. These manuals are a critical component of PASAI's support to developing SAIs in the region to assist them to complete high-quality audits. These manuals are part of the support and services PASAI offers to the SAIs of the region to enable the achievement of Strategic Priority 3 (SP3) of PASAI's Strategic Plan 2014-2024 which is aimed at achieving high-quality audits. These manuals alone will, however, not result in high-quality audits. It is essential that each SAI takes this manual and develops their own customised audit manual to ensure compliance with the International Standards of Auditing, whether that be ISSAIs, ISA, or GAGAS, that is relevant to their SAI. This manual has two components:

- PASAI Regional Audit Manual; and
- Case Study materials - including templates.

In the Pacific, most developing SAIs, due to a lack of resources and expertise, find it difficult to keep their audit manuals aligned with auditing standards, particularly given the rapid pace of change in recent years. The objective of the manuals in this suite is to provide guidance to help SAIs develop an approach to firstly customise the audit manuals so that they align to the requirements and realities of the SAI's unique operating environment. This will make the manuals more useful to the specific situation and needs of each SAI. PASAI is planning to provide support to SAIs through a workshop and SAI level support to ensure this important customisation phase is achieved and that the effectiveness of the regional manual is maximised.

The next and crucial step is to provide ongoing support to ensure the SAI manual remains consistent with SAI's implementation of the audit methodology as it used in conducting the related audits. PASAI will also ensure that SAIs are informed of changes to Standards so that their customised manuals remain aligned to the latest updates to auditing standards.

In addition, to assist with making the manuals useful and relevant, they incorporate templates, checklists, examples, and case studies intended to serve as useful aids to understanding the standards and approaches. Each of these components and PASAI's ongoing support is intended to result in a more sustainable outcome.

PASAI is encouraged by the commitment of SAIs to raise standards. The PASAI Governing Board has clearly heard from SAIs across the region the utmost dedication to raising SAI standards because of the SAIs commitment to providing high quality audit so that governance and accountability systems in their countries can be improved and the lives of citizens positively impacted

We take this opportunity to express our appreciation to the reviewers and experts working in SAIs within the Pacific region and Internationally (IDI) for their contributions and comments in the development of these manuals. They are acknowledged specifically within each Audit Manual.

John Ryan
Secretary-General of PASAI
Controller and Auditor-General of New Zealand

Acknowledgements

Martin Grimwood was PASAI's consultant engaged to develop the Audit manuals. He has worked extensively throughout the region being a former Auditor-General of Tuvalu and Deputy Auditor-General of Solomon Islands. He has also been Adviser and Mentor to the Office of the Auditor-General of Vanuatu and has just (December 2019) concluded a similar role in Solomon Islands.



Martin holds a joint honours degree in Accounting and Law from the University of Southampton and was awarded his Masters degree by the University of Bath for his pioneering research into the use of Qualitative Methods in Performance Auditing. He holds professional accounting qualifications with the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Association of Certified Accountants (CACA); he is also a qualified Company Secretary (ICSA).

He was a founder member of the original South Pacific Association of Supreme Audit Institutions (SPASAI) which was part of the Commonwealth Training Initiative (CTI) which arose from the 1986 Commonwealth Auditors-General conference in Ottawa under the chairmanship of Ken Dye. He was also involved developing the three-volume audit manual which was also part of the CTI.

In addition to his work in the Pacific Region, Martin has worked with Supreme Audit Institutions (SAI) in many countries including establishing the SAI in Bosnia-Herzegovina and Afghanistan.

The following are also to be acknowledge for reviewing the draft manual and providing feedback to PASAI's Consultant:

- Mrs. Sarah Markley, PASAI Deputy Secretary-General
- Mr Tiofilusi Tiueti, PASAI Chief Executive
- Mrs A'eau Agnes Aruwafu, former PASAI Director Technical Support
- Md Shofiquil Islam IDI Senior Manager, Professional and Relevant SAIs' Department

Also, to thank the Communication Unit of SAI New Zealand for making the manuals more user friendly through the formatting of the manuals to brand them as PASAIs.

Finally, PASAI Acknowledges the support of development partners in making it possible for the development of these Regional Audit Manuals



Copyright statement

This manual is the copyright of PASAI, a regional organisation of the International Organisation of Supreme Audit Institutions (INTOSAI).

Disclaimer statements

This manual has been developed by PASAI as a resource for SAIs in the Pacific region to help customise their own audit manuals.

The use of the manual is the responsibility of each individual SAI, having regard to its mandate, capacity and country circumstances. PASAI disclaims any responsibility or liability, where direct or indirect as a consequence of the use or application of this manual.

Version updates

It is important that records are kept of any major updates to the PASAI Regional Performance Audit manual:

Version	Details of updates made	Revised version issued	Signed off through GB approval (GB paper reference, dates, details)

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ACRONYMS

AFROSAI-E	African Organisation of Supreme Audit Institutions – English Speaking
AFS	Annual Financial Statements
ANAO	Australian National Audit Office
AR	Audit Risk
CAAT	Computer Assisted Audit Technique
CACA	Chartered Association of Certified Accountants
CIPFA	Chartered Institute of Public Finance and Accountancy
CNMI	Commonwealth of the Northern Marianas Islands
CTI	Commonwealth Training Initiative
CoCo	Criteria of Control Board, Canada
COSO	Committee of Sponsoring Organizations
CR	Control Risk
DR	Detection Risk
DST	Direct Substantive Testing
ECA	European Court of Auditors
FRF	Financial Reporting Framework
FSM	Federated States of Micronesia
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GAGAS	Generally Accepted Government Auditing Standards
GASB	Government Accounting Standards Board
GBA	Gender-Based Analysis
GFM	Government Financial Management
GPFS	General Purpose Financial Statements
GRB	Gender-Responsive Budgeting
IAS	International Accounting Standard(s)
IASB	International Accounting Standards Board
ICE	Intensive Care Equipment
ICQ	Internal Control Questionnaire
ICSA	Institute of Chartered Secretaries and Administrators
IDI	INTOSAI Development Initiative
IFAC	International Federation of Accountants
IFPP	INTOSAI Framework of Professional Pronouncements
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standards
INTOSAI	International Organisation of Supreme Audit Institutions
INTOSAI – P	INTOSAI -
INTOSAI GUID	INTOSAI - Guidelines
IPSAS	International Public Sector Accounting Standards
IPSASB	IPSAS Board

IR	Inherent Risk
ISA	International Standard on Auditing
ISSAI	International Standards for Supreme Audit Institutions
MoFPED	Ministry of Finance, Planning and Economic Development
MPE	Maximum Potential Error
MPER	Maximum Potential Error Rate
NAO	National Audit Office
NSW	New South Wales
NZ	New Zealand
PASAI	Pacific Association of Supreme Audit Institutions
PFM	Public Financial Management
PN	Practice Notes
PPE	Personal Protective Equipment
PPR	Public Procurement Rules
QA	Quality Assurance
QAO	Queensland Audit Office
QARC	Quality Assurance Review Committee
QC	Quality Control
QLD	Queensland
SAI	Supreme Audit Institution
SAI PMF	SAI Performance Measurement Framework
SBA	Systems Based Approach
SEC	Security and Exchange Commission
SIC	Standards Interpretation Committee
SOE	State-Owned Enterprise
TA	Technical Assistance
TER	Tolerable Error Rate
VIC	Victoria
WP	Working Papers
WPF	Working Papers Files

PART ONE: INTRODUCTION

Chapter 1: Introduction

1.1 The New Series of PASAI Manuals

Previous Pacific Association of Supreme Audit Institutions (PASAI) manual and guidelines were produced by committees drawn from member countries including reliance on other regional audit manuals.

This process provided valuable capacity development for those involved in the development process. During the process a valuable partnership with AFROSAI-E was developed which continued during the drafting of this new manual.

PASAI faces ongoing challenges to facilitate Supreme Audit Institute (SAI) engagement with materials provided as resources to the region. The second half of the current PASAI strategy was identified as the right time to refresh the initial manual work and to seek to use approaches that may, more successfully, ensure the wealth of guidance contained in the manuals is used to best effect

Furthermore, PASAI's aim to become a Learning and Knowledge institution has led to the decision to enhance and develop the regional manuals for all streams of audit - Financial Audit, Compliance Audit and Performance Audit.

Accordingly, an audit expert was selected, after an open tender process, to develop these PASAI audit manuals and to work with the PASAI Secretariat to ensure this manual reflects what is relevant for our PASAI region and its members. Details of the consultant and those involved in reviewing and providing input into these manuals are included in the **Acknowledgements Section**.

In support of the manual there is also a separate volume containing case study materials.

As we make clear below, the target is for every SAI to customise this manual for their own unique environment in order to maximise the effectiveness of the content.

These manuals are designed for use by developing countries. However, the manuals should be of use to developed countries to complement their own systems and processes. It is PASAI's expectation that developed SAI would draw on the customised versions of this material when working to support their twinning partners.

The manuals do not describe the various judicial systems as these are very country-specific; however, PASAI may develop such manuals in future. This is due to only two of our member SAIs under such system and they already have an established guidelines. However, the manuals sit outside and complement a local understanding of specific jurisdictional frameworks which can be recognised through the customisation of the manual materials.

1.2 PASAI Region

The PASAI region covers the island states of Oceania together with New Zealand, Australia and some Australian states (see map).



Table 1 below provides more details of PASAI membership together with a further link to each member.

Table 1: PASAI Membership

	Member	PASAI Link	SAI Website
1	American Samoa	www.pasai.org/american-samoa	www.americansamoa.gov/territorial-audit-office
2	Australia - NAO	www.pasai.org/australia	www.anao.gov.au
3	Australia - NSW	www.pasai.org/new-south-wales	www.audit.nsw.gov.au/
4	Australia - QLD	www.pasai.org/queensland	www.qao.qld.gov.au
5	Australia - VIC	www.pasai.org/victoria	www.audit.vic.gov.au
6	Cook Islands	www.pasai.org/cook-islands	www.auditoffice.gov.ck
7	Federated States of Micronesia (FSM) – National Office	www.pasai.org/federated-states-of-micronesia-national-office	www.fsmopa.fm/

8	FSM - Chuuk	www.pasai.org/federated-states-of-micronesia-chuuk	No website
9	FSM - Kosrae	www.pasai.org/kosrae	No website
10	FSM - Pohnpei	www.pasai.org/pohnpei	www.opapni.fm
11	FSM - Yap	www.pasai.org/yap	www.audityap.org
12	French Polynesia	www.pasai.org/french-polynesia	www.ccomptes.fr/polynesie-francaise
13	Guam	www.pasai.org/guam	www.opaguam.org
14	Kiribati	www.pasai.org/kiribati	kao.gov.ki
15	Marshall Islands	www.pasai.org/marshall-islands	www.rmioag.com/
16	Nauru	www.pasai.org/nauru	No website
17	New Caledonia	www.pasai.org/new-caledonia	See footnote ¹
18	New Zealand	www.pasai.org/new-zealand	www.oag.govt.nz
19	Commonwealth of the Northern Marianas Islands	www.pasai.org/northern-mariana-islands	www.opacnmi.com
20	Palau	www.pasai.org/palau	www.palauopa.org
21	Papua New Guinea	www.pasai.org/papua-new-guinea	www.ago.gov.pg
22	Republic of Fiji	www.pasai.org/fiji-islands	www.oag.gov.fj
23	Samoa	www.pasai.org/samoa	www.audit.gov.ws
24	Solomon Islands	www.pasai.org/solomon-islands	www.oag.gov.sb
25	Tonga	www.pasai.org/tonga	www.audit.gov.to
26	Tuvalu	www.pasai.org/tuvalu	www.tuvaluaudit.tv
27	Vanuatu	www.pasai.org/vanuatu	www.nao.gov.vu

SAI in the PASAI region operate under three distinct models:

- **Legislative-Parliamentary (Commonwealth System):** under this system the work of the SAI is linked closely with that of parliamentary accountability with reports presented to the Speaker for tabling before the House. It is usual to have a (Public Accounts) Committee of parliament to review the reports and to issue their own report to the House. Such SAI are called “Office of the Auditor-General” or “National Audit Office” and are usually headed by a single person (often the Auditor-General) and are primarily staffed by accountants and auditors. They focus primarily of financial and performance audits.

The countries using this system comprise: Australia (and states); Cook Islands, Fiji, Kiribati, Nauru, New Zealand, Papua New Guinea, Samoa, Solomon Islands, Tonga, Tuvalu and Vanuatu;

¹ www.ccomptes.fr/fr/CTC01/Accueil.html
<http://www.ccomptes.fr/index.php/Nos-activites/Chambres-territoriales-des-comptes-CTC/Nouvelle-Caledonie>

- **Legislative-Congressional Model (United States System):** the SAI's work is closely related to the legislative obligations of government with reports presented to the Speaker, Governor and relevant agencies. Typically, the SAI is called "the Office of the Public Auditor" and is headed by the "Public Auditor" who is appointed by the Governor with the legislature's support. The SAI focuses mainly on performance and forensic audit work with the financial audits contracted out to the private sector. Staff tend to have investigative and generalist background rather than being professional accountants. The SAI reports either to the legislature or another public oversight body.

The countries using this system comprise: American Samoa, Commonwealth of the Northern Marianas Islands, Federated States of Micronesia and each of its states (Chuuk, Kosrae, Pohnpei and Yap), Guam, Marshall Islands and Palau.

- **Judicial Model (French System):** The SAI is an integral part of the judicial system, operating independently from the executive and legislative branches. The SAI is usually known as the Court of Accounts (or Audit) and its members are judges, typically appointed for an unlimited time. The work focuses on financial and performance audits with specific attention being paid to the legality of the transactions. Staff have legal or generalist backgrounds. There is not usually any parliamentary committee to which the court reports. The court itself holds officials to account and can impose penalties on audited officials.

The countries using this system: French Polynesia and New Caledonia.

The different models give rise to different accounting and auditing standards used in the different jurisdictions.

However, whilst there are different **Auditing Standards** all PASAI members are also members of the International Organisation of Supreme Audit Institutions (INTOSAI) – either as full members (the majority); as an affiliate (Guam) or through the "colonial power": France (French Polynesia and New Caledonia) and the United States (American Samoa and Commonwealth of the Northern Marianas Islands). This means that they are encouraged to comply with the International Standards of Supreme Audit Institutions (ISSAI), if they do not have an authoritative body that sets the auditing standards for the government.

Those countries following the **Legislative-Congressional Model** also have to be compliant with the Generally Accepted Government Auditing Standards (GAGAS) (the "Yellow Book"). These standards are not significantly different from the IPSAS.

Given that all PASAI members are encouraged to follow ISSAI they will be the prime reference in this manual. However, where indicated, the appropriate countries will need to customise the manual by adding the reference to GAGAS or other applicable local standards.

1.3 Customisation

Whilst in the past every manual and guideline produced by PASAI was intended to be customised by individual Supreme Audit Institutions (SAI), we are aware that detailed customisation did not occur. Therefore PASAI has with this redevelopment of our regional manuals specifically provided for assistance to be given to SAIs so that, together with a regional workshop to assist SAIs to customise manuals, we will provide guidance in this manual on how customisation should be done to maximise the effectiveness of this material.

It is clear that, given the different models of auditing followed by PASAI members, customisation is essential. The idea of a “one size fits all” manual is outdated and we want to ensure that the investment in these new manuals maximises their usefulness to our members.

The three new manuals and templates² seek to solve this problem in three main ways:

- **Manuals and Templates:** the manuals make it very clear where sections should be subject to customisation;
- **Training:** we will be providing training to our SAIs as to the content of each manual; and
- **Pilot Audits:** PASAI will coordinate and evaluate individual customised manuals and refine them as necessary by encouraging SAIs to conduct pilot audits to ‘test’ the manuals before finalising it.

1.4 SAI Overall Approach to Capacity Building

In December 2016, INTOSAI endorsed the Supreme Audit Institutions Performance Measurement Framework³ (SAI PMF) as an approved tool for use by its members. The SAI PMF provides SAI with a framework for voluntary assessments of their performance against the International Standards for Supreme Audit Institutions (ISSAIs) and other established international good practices for external public auditing.

SAI PMF is a multi-purpose, universal framework, and can be applied in all types of SAI, regardless of governance structure, mandate, national context and development level and, thus, has been used by PASAI across its members. The SAI PMF programme kickstarted in 2015 and through a multi-phased approach over the years, PASAI has coordinated the completion of SAI PMF assessments of almost all Pacific SAIs.

² This volume does not have templates only a case study as a separate volume.
³ See: <https://www.idi.no/en/idi-cpd/sai-pmf>

Figure 1: SAI Performance Measurement Framework

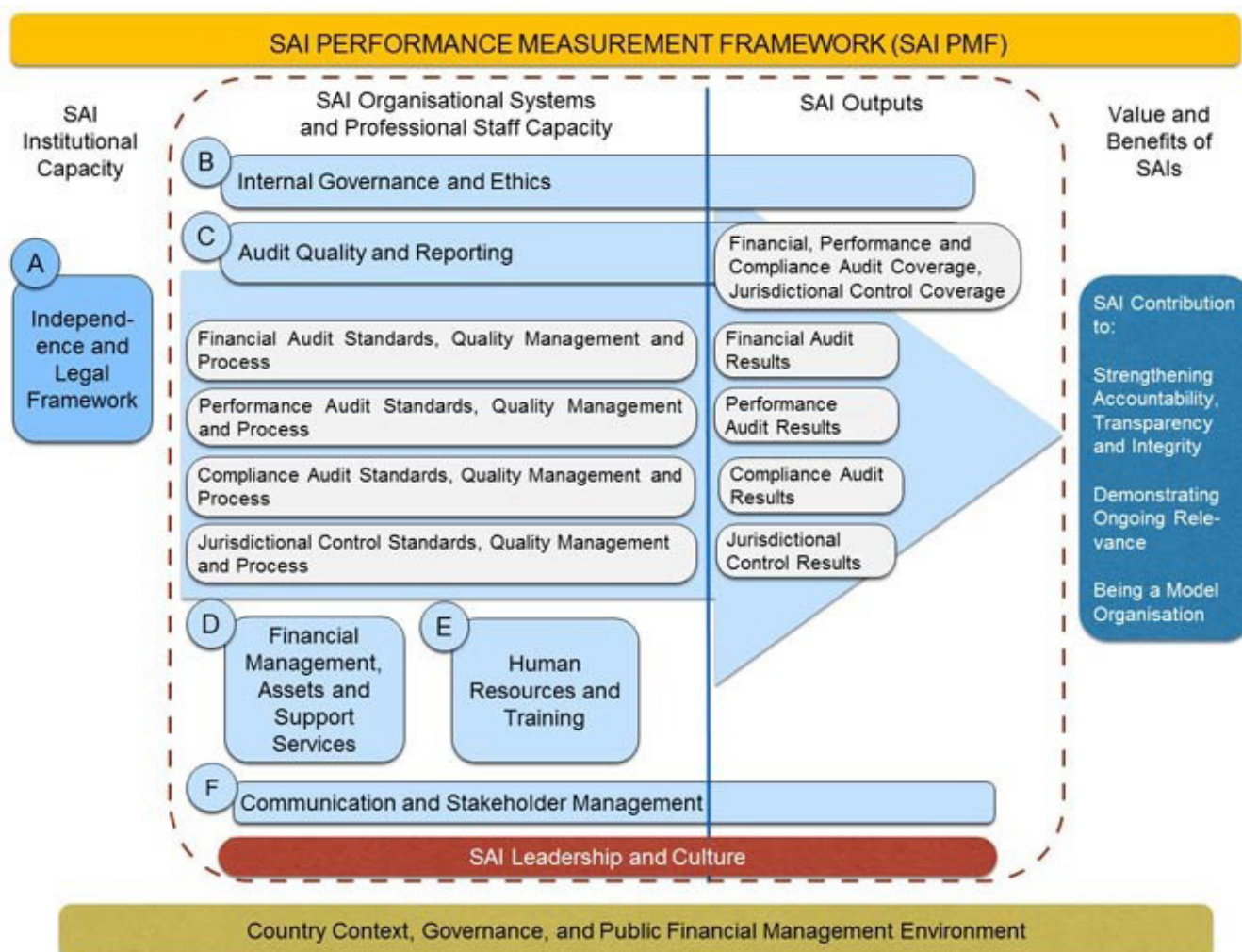


Table 2 indicates the numbers of Domains, Performance Indicators, Dimensions and Tests.

Table 2: Analysis of Domains, Performance Indicators, Dimensions and Criteria

Area	Number of Items
Domain	6
Performance Indicators	25 ⁴
Dimensions	805
Tests	560

Domain “C” covers Audit Quality and Reporting. The table below indicates the key performance indicators and dimensions for Compliance Audits.

Table 3: Extract from SAI PMF Domain “C”

Performance Indicator	Dimension
SAI-15: Compliance Audit Standards and Quality Management	(i) Compliance Audit Standards and Policies (ii) Compliance Audit Team Management and Skills (iii) Quality Control in Compliance Audit
SAI-16: Compliance Audit Process	(i) Planning Compliance Audits (ii) Implementing Compliance Audits (iii) Evaluating Audit Evidence, Concluding and Reporting in Compliance Audits
SAI-17: Compliance Audit Results	(i) Timely Submission of Compliance Audit Results (ii) Timely Publication of Compliance Audit Results (iii) SAI Follow-up on Implementation of Compliance Audit Observations and Recommendations

This manual is intended to ensure that any SAI following it in its entirety will score very highly when answering the associated SAI PMF test questions.

1.5 Finalisation of Audit Manuals

For each SAI the final draft manuals which arise from the Capacity Building training sessions, will be subject to rigorous testing before being finally adopted.

“Pilot audits” will use the draft manuals as the basis for undertaking actual audit work. The methodology laid down in the manuals will be tested for its practicality and any problems identified. The draft manuals will then be updated and finalised on the basis of such feedback.

We **recommend** at least three pilot audits be used in each SAI to test each manual.

PASAI will co-ordinate the process of ensuring technical support is provided to each member to enable the pilot audits to be undertaken. This will be in the form of a blended approach which can be either a regional workshop, SAI level support or engaging a TA.

1.6 Keeping Audit Manuals Relevant

PASAI will provide each SAI with regular bulletins setting out developments which affect the effectiveness of the manual. This will be done by both e-mails and social media.

This will include not only the results of our own research but also relevant material produced by the International Organisation of Supreme Audit Institutions (INTOSAI); other regional SAI bodies; the INTOSAI Development Initiative (IDI); International Federation of Accountants (IFAC); national SAI; and any other relevant sources

These bulletins will indicate areas where the individual members manuals need reviewing and, where appropriate, will provide new text which can be used for the updating process.

Any significant changes to the PASAI Audit manual will be submitted to the PASAI Governing Board (meet bi-annually) for approval and then included in a revised version of the manual. This will be recorded as per the table on page 4.

1.7 Structure of this Manual

The manual comprises four main parts:

- [Part Two](#): The Background to Compliance Auditing: this part examines the framework within which the compliance takes place;
- [Part Three](#): Types of Compliance Auditing:
 - Compliance Audit as Part of the Financial Audit Process (ISSAI #4200): this part covers using Compliance Audits to support the formation of an opinion on the Annual Financial Statements (AFS);
 - Stand Alone Compliance Audits (ISSAI #4100): covers the situation where the report on a compliance audit is a “stand-alone” product in its own right;
 - Compliance Audits under a Judiciary Approach (ISSAI #4300 (draft): to be used for those SAI which follow the Judicial Model (French System);
 - Compliance Audits under the Legislative-Congressional Model (United States System): for Compliance Audits which follow the Government Auditing Standards (the “Yellow Book”) of the General Accounting - “Standards for Attestation Engagements and Reviews of Financial Statements”.
- [Part Four](#): Common Methodologies: whilst audit planning and reporting are tailored more to the type of compliance auditing and are included in the relevant section of Part Three, there are some methodologies – notably assurance, evidence gathering and documentation, follow-up and quality assurance which are common to all forms of compliance audit. These are recorded in this part to avoid unnecessary duplication;
- [Part Five](#): Next Steps: covers action needed vis a vis the manual.

In the Financial Auditing Manual there were, at the start of each main chapter, three text boxes:

Key Points: This box will indicate the key points in the chapter and provide hyperlinks thereto.

Internet Links: This box will indicate the key internet links contained in the chapter.

Customisation: This box will provide advice on customising the chapter.

As, in this manual, the only relevant **Internet Links** are those to the audit standards, this box has been omitted from this manual.

Similarly, for **Customisation**, as each box would have been identical and, as the process is covered in Chapter #13, these boxes have also been omitted from this volume.

PART TWO: BACKGROUND TO COMPLIANCE AUDIT

Chapter 2: Overview of Compliance Auditing

2.1 What is a Compliance Audit?

Laws and regulations set out what activities public sector entities are charged with carrying out for citizens, the overall objectives to be achieved and how the due process rights of individual citizens are protected. Public funds are entrusted to public sector entities for their proper management. It is the responsibility of these public sector bodies and their officials to be transparent about their actions, accountable to the citizens for the funds with which they are entrusted, and to exercise good stewardship over such funds.

Figure 2: Authorities



The role of public sector auditors is to help Parliament in monitoring how the basic principles of compliance are being followed and applied. In the context of **compliance auditing**, this responsibility includes **determining whether information related to a particular subject matter is in compliance, in all material respects, with relevant criteria such as laws, regulations, directives, terms of contracts and agreements, etc.**

The results of such audits are reported to the audited entity and to the legislature. In addition, the results are normally made available to the general public. This is done to support accountability and transparency in the public sector.

The management of the public sector entities is accountable for operating in accordance with the provisions of the relevant laws and regulations.

Since legislation is the primary means by which legislators control the raising and spending of money by the public sector, **compliance audits are an important and integral part of the audit mandate**, or terms of engagement, for most audits of public sector entities.

Compliance auditing is performed by assessing whether activities, financial transactions and information are, in all material respects, in compliance with the authorities which govern the audited entity. These authorities may include rules, laws and regulations, budgetary resolutions, policy, established codes, agreed terms or the general principles governing sound public-sector financial management and the conduct of public officials.

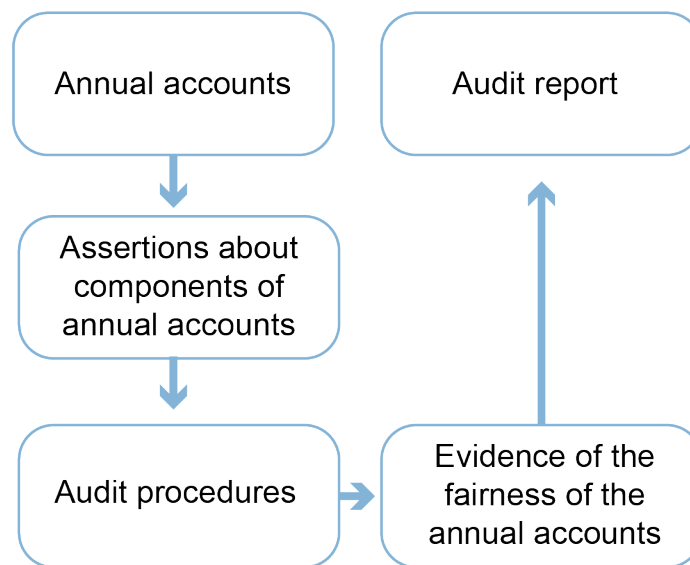
The relationship between Financial and Compliance Audit is illustrated in Table 3.

Table 3: Relationship between Financial and Compliance Audit

	Financial Audits	Compliance Audits	
Subject	Reliability of the annual annual accounts	Legality and regularity of underlying transactions	Compliance with applicable laws and regulations for selected topic
	Effectiveness of internal control systems		
	Recurrent tasks: audit programme for these audits remains generally unchanged from year to year	Selected task: audit programme depends on the specific objective of the audit	
	Recurrent or selected task		
Task substance	Examine accounts, determine if they give a true and fair view	Review procedures and financial records to determine whether laws, regulations, rules and procedures set out by legislation are being followed; test the reality and legality of underlying transactions	
	Test systems to determine if they are effective for purpose (reliability or compliance)		
Assertions	Occurrence; completeness; accuracy; cut-off; classification; legality and regularity; existence; rights and obligations; valuation and allocation. Distinguish between events for the period, those at period end, and presentation	Occurrence; completeness; accuracy; cut-off; existence; rights and obligations; valuation; and eligibility.	Depends on the audit objective(s)
	Proper design, maintenance and continuous effective operation of systems		

Source: ECA Financial and Compliance Audit Manual

The relationship between Accounts, Evidence and the Audit Report appears in Figure 3.

Figure 3: Relationship between Accounts, Evidence and the Audit Report

Source: ICA Financial and Compliance Audit Manual

2.2 International Standards for Supreme Audit Institutions (ISSAI)⁵

There are three blocks of ISSAI specifically applicable to Compliance Auditing:

- **ISSAI #400-499:** Compliance Auditing Principles;
- **ISSAI #4000-4899:** Compliance Audit Standards; and
- **GUID 4900-4999:** Supplementary Compliance Audit Guidelines.

There is no substitute for reading them in full but they are discussed in a summary format in the chapters below.

2.3 Types of Compliance Audit

Based on the ISSAI (plus Generally Accepted Auditing Standards (GAAS)), we will be recognising four types of compliance audit each of which will have their own part for ease of reference.

The four types are:

- **Compliance Audit as Part of the Financial Audit Process;**
- **Stand Alone Compliance Audits;**
- **Compliance Audits under a Judiciary Approach;** and
- **Compliance Audits under the Legislative-Congressional Model (GAAS).⁶**

2.4 Importance of Compliance Audit in the Public Sector

As stated in ISSAI #100.18, public sector auditing can be described as a systematic process of objectively obtaining and evaluating evidence to determine whether information or actual conditions conform to established criteria.

The definition of Compliance Audit builds on this definition, with a specific focus on assessing compliance with criteria derived from authorities. Compliance Audit is an

⁵ <https://www.issai.org/professional-pronouncements/?n=0-1000000000>
⁶ Google "AU section 801 of AICPA Professional Standards" for downloadable version.

independent assessment of whether a given subject matter is in compliance with criteria identified by applicable authorities.

The concept and establishment of audit is inherent in public financial administration, as the management of public funds represents a trust. According to ISSAI #400.16, it is the responsibility of public sector bodies and their appointed officials to be transparent about their actions and accountable to citizens for the funds with which they are entrusted, and to exercise good governance over those funds.

Auditors assess whether activities, financial transactions, and information are, in all material respects, in compliance with the authorities which govern the audited entity as per ISSAI #400.12. In compliance audit, auditors look for material deviations or departures from established criteria which could be based on laws and regulations, principles of sound financial management, or propriety.

Compliance Audit plays an important role in ensuring that the principles of transparency, accountability and good governance are actually met:

- **Transparency:** promotes This by providing reliable reports as to whether public funds have been utilised in line with the requirements set by applicable authorities;
- **Accountability:** promotes this by reporting deviations from and violations of authorities. This information makes it possible to take corrective action, and to hold public officials accountable for their activities; and
- **Good Governance:** promotes this by identifying weaknesses and deviations from laws and regulations, and also by assessing the propriety of officials.

2.5 Standard Methodology – Audit Practice

In implementing the Compliance Audit, the auditor focuses on preparing and timely delivering the following main practices and procedures generally:

- **Initial Considerations:**
 - Determine compliance audit scope;
 - Consider principles with ethical significance (e.g. independence and objectivity); and
 - Ensure that quality control procedure is in place.
- **Planning the Audit:**
 - Determine the elements of the audit;
 - Identify subject matter and criteria;
 - Understand the entity and environment;
 - Develop audit strategy and plan;
 - Understand internal control;
 - Establish materiality for planning purpose;
 - Assess risk;
 - Plan audit procedure to enable reasonable assurance; and
 - Consider non-compliance that may indicate suspected unlawful acts.
- **Performing the Audit and Gathering Evidence:**
 - Gather evidence through various means; and

- Continually update planning and risk assessment.
- **Evaluating Evidence and Forming Conclusion:**
 - Evaluate whether sufficient appropriate evidence obtained;
 - Consider materiality for reporting purpose;
 - Form conclusions;
 - Obtain written representations as necessary; and
 - Address subsequent events as necessary.
- **Reporting**
 - Prepare reports;
 - Include recommendations and responses from entity as appropriate; and
 - Follow-up the reports as necessary.

Chapter 3: General Principles and Introduction to Compliance Auditing

General Principles and Introduction to Compliance Auditing according to INTOSAI Auditing Standards and Best Practice (ISSAI #400 and ISSAI #4000)

This chapter provides details on: [How does the ISSAI Framework help in the Conduct of Quality Compliance Audits?](#); [Compliance Auditing Principles \(ISSAI #400\)](#); [Compliance Auditing Standards: ISSAI #4000 to #4899](#); and [GUID 4900 - 4999: Supplementary Compliance Audit Guidelines](#).

3.1 Introduction

To fulfill the requirements of compliance audit standards, the SAI must assess its compliance audit practice against the compliance audit standard requirements against which SAI performance is measured.⁷

ISSAI #400 describes the principles of compliance auditing. These principles are fundamental to the conduct of a compliance audit. As the nature of the audit is iterative and cumulative, the auditor should consider these principles prior to the commencement of any audit and throughout the audit process, including in the planning and designing, gathering and evaluating evidence and reporting phases.

The fundamental principles are grouped by principles related to the SAI's organisational requirements - the General Principles (GP),⁸ as well as the principles related to specific steps in the audit process such as planning, conducting and reporting.

The Fundamental Auditing Principles set out principles with **ethical significance** that are taken into consideration prior to commencing the audit (ISSAI 200, 2.2.1). These principles relate to:

- a) The independence of the SAI and the auditor, including political neutrality;
- b) Avoidance of conflict of interest between the auditor and the audited entity;
- c) The need for the auditor and the SAI to possess the necessary competence; and
- d) Exercise of due care and concern by the SAI and the auditor in complying with the Fundamental Auditing Principles.

If for some reason, the SAI or the auditor is not in a position to comply with the Fundamental Auditing Principles that have ethical significance, appropriate actions are taken to ensure that the threats to non-compliance are eliminated before commencing the audit. This may, for example, involve re-allocating staff assigned to the audit, additional training or involvement of experts.

As with other types of auditing, it is important in performing compliance audits that the SAI have processes and procedures in place to ensure that the work carried out is of **sufficient quality**, that the public sector auditors performing such audits collectively have the necessary competence and skills, and that the work of the team is appropriately directed, supervised and reviewed. INTOSAI's Fundamental Auditing Principles establish benchmarks and provide guidance for ensuring the quality of work.

3.2 How does the ISSAI Framework help in the Conduct of Quality Compliance Audits?

The International Standards of Supreme Audit Institutions (ISSAI) on compliance auditing are broad principles, standards, and guidelines that provide a common frame of reference for SAI and facilitate convergence towards common professional standards and practices of compliance audit.

In practice, many SAI carry out an annual audit that includes different types of audit or as a combination of financial, compliance or performance audits. ISSAI #100 states that SAIs may conduct combined audits incorporating financial, performance and/or compliance aspects.⁹

Some SAI conduct compliance audits as a standalone engagement. This means that the Compliance Audit is done on its own and it is not done in conjunction with financial auditing or performance auditing. The ISSAI provide that compliance auditing may be planned, performed and reported separately from audit of financial statements and from performance audits. It may be conducted on a regular or ad-hoc basis, as distinct and clearly defined audits related to specific subject matters.¹⁰

Many SAI follow a practice of combining their audit of financial statements with giving assurance on compliance issues within one audit process. Compliance auditing is much broader than financial auditing and enables the auditor to have a wider scope. The legislature, as an element of public democratic process, establishes the priorities for public sector income and expenditure and for the calculation and attribution of expenditure and income. The underlying premise of legislative bodies, and the decisions that they take, are the source of the authorities governing cash flow in the public sector. Compliance with those authorities constitutes a broader perspective alongside the audit of financial statements in budgetary execution.

When Compliance Auditing is part of a Performance Audit, compliance is seen as one of the aspects of economy, efficiency and effectiveness, as stated in ISSAI #400.26. In combined audits of this kind, auditors should use their professional judgment in deciding whether performance or compliance is the primary focus of the audit and determine audit scope and criteria accordingly.

3.3 Principles of Compliance Auditing (ISSAI #400)

3.3.1 General Principles

Figure 4 summarises the General Principles of Compliance Auditing.

Figure 4: General Principles of Compliance Auditing



Source: The figure is inspired by the ID INTOSAI ISSAI Implementation supporting handbooks and documents on the three types of audit according to the INTOSAI and ISSAI

Implementing ISSAI allows the SAI's beneficiaries to receive and implement practical audit guidance and methodologies at each of the three main phases of the audit process (planning, execution and reporting), according to INTOSAI and ISSAI.

In practice, adopting the ISSAI, including the "Fundamental principles of Compliance Auditing" standard, will ensure the functioning of the required SAI core process under the INTOSAI and ISSAI. These principles need to be followed prior to commencement of an audit and also throughout the audit process.

3.3.2 Overview

ISSAI #400 constitutes the basis for compliance auditing principles in accordance with the ISSAI. This standard provides detailed information on the following:

- the purpose and authority of the ISSAI on compliance auditing;
- the compliance auditing framework and the different ways in which audits are conducted;
- the elements of compliance auditing; and
- the principles of compliance auditing.

3.3.3 Purpose and Authority (Paragraph #4 et seq.)

The purpose of the ISSAI on compliance auditing is to provide a comprehensive set of principles, standards and guidelines for the compliance auditing of subject matter, both qualitative and quantitative, that varies widely in scope and can be addressed through a range of audit approaches and reporting formats.

3.3.4 Compliance Auditing Framework (Paragraph #12 et seq.)

The Objective of Compliance Auditing

Compliance auditing is the independent assessment of whether a given subject matter is in compliance with applicable authorities identified as criteria. Compliance audits are carried out by assessing whether activities, financial transactions and information comply, in all material respects, with the authorities which govern the audited entity.

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.

Characteristics of Compliance Auditing

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.

Compliance auditing is often an integral part of an SAI's mandate for the audit of public-sector entities. This is because legislation and other authorities are the primary means by which legislatures exercise control of income and expenditure, management and the rights of citizens to due process in their relations with the public sector. Public-sector entities are entrusted with the sound management of public funds. It is the responsibility of public-sector bodies and their appointed officials to be **transparent** about their actions and **accountable**

to citizens for the funds with which they are entrusted, and to exercise **good governance** over those funds.

Compliance auditing promotes **transparency** by providing reliable reports as to whether funds have been administered, management exercised and citizens' rights to due process honoured as required by the applicable authorities. It promotes **accountability** by reporting deviations from and violations of authorities, so that corrective action may be taken and those accountable may be held responsible for their actions. It promotes **good governance** both by identifying weaknesses and deviations from laws and regulations and by assessing propriety where there are insufficient or inadequate laws and regulations. Fraud and corruption are, by their very nature, elements which counteract transparency, accountability and good stewardship.

Compliance auditing therefore promotes good governance in the public sector by considering the risk of fraud in relation to compliance.

The different Perspectives of Compliance Auditing

Compliance auditing can be part of a combined audit that may also include other aspects.

Though other possibilities exist, compliance auditing is generally conducted either:

- in relation with the audit of financial statements (see ISSAI #4200 for additional guidance in this regard), or
- separately from the audit of financial statements (see ISSAI #4100), or
- in combination with performance auditing.

3.3.5 Elements of Compliance Auditing (Paragraph #27 et seq.)

Authorities and Criteria

Authorities are the most fundamental element of compliance auditing, since the structure and content of authorities furnish the audit criteria and therefore form the basis of how the audit is to proceed under a specific constitutional arrangement.

Authorities may include rules, laws and regulations, budgetary resolutions, policy, established codes, agreed terms or the general principles governing sound public-sector financial management and the conduct of public officials. Most authorities originate in the basic premises and decisions of the national legislature, but they may be issued at a lower level in the organisational structure of the public sector.

Criteria are the benchmarks used to evaluate or measure the subject matter consistently and reasonably. The auditor identifies criteria on the basis of the relevant authorities. To be suitable, compliance audit criteria must be relevant, reliable, complete, objective, understandable, comparable, acceptable and available. Without the frame of reference provided by suitable criteria, any conclusion is open to individual interpretation and misunderstanding.

Subject Matter

The subject matter of a compliance audit is defined in the scope of the audit. It may take the form of activities, financial transactions or information. For attestation engagements on compliance it is more relevant to identify the subject matter information, which may be a statement of compliance prepared in accordance with an established and standardised reporting framework.

The Three Parties in Compliance Auditing

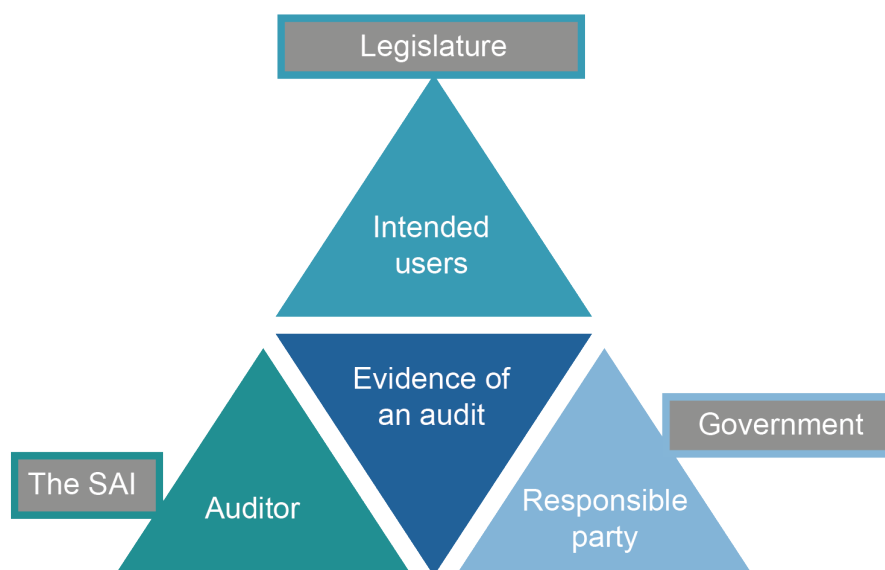
Compliance auditing is based on a three-party relationship in which **the auditor** aims to obtain sufficient appropriate audit evidence in order to express a conclusion designed to enhance the degree of confidence of **the intended users**, other than **the responsible party**, about the measurement or evaluation of a subject matter against criteria.

In compliance auditing the responsibility of **the auditor** is to identify the elements of the audit, assess whether a particular subject matter is compliant with the established criteria and issue a compliance audit report.

The responsible party is the executive branch of government and/or its underlying hierarchy of public officials and entities responsible for the management of public funds and the exercise of authority under the control of the legislature. The responsible party in compliance auditing is responsible for the subject matter of the audit.

The intended users are the individuals, organisations or classes thereof for whom the auditor prepares the audit report. In compliance auditing the users generally include the legislature as representatives of the people, who are the ultimate users of compliance audit reports. The legislature makes decisions and sets priorities concerning the calculation and purpose of public-sector expenditure and income. The primary user in compliance auditing is often the entity that issued the authorities identified as audit criteria.

Figure 5: Three Parties to an Audit



3.3.6 Assurance in Compliance Auditing (Paragraph #40 et seq.)

An auditor performs procedures to reduce or manage the risk of providing incorrect conclusions, recognising that, owing to the inherent limitations in all audits, no audit can ever provide absolute assurance of the condition of the subject matter. This should be communicated in a transparent way. In most cases, a compliance audit will not cover all elements of the subject matter but will rely on a degree of qualitative or quantitative sampling.

Compliance auditing carried out by obtaining assurance enhances the confidence of the intended users in the information provided by the auditor or another party.

In compliance auditing there are **two levels of assurance: reasonable assurance,**

conveying that, in the auditor’s opinion, the subject matter is or is not in compliance, in all material respects, with the stated criteria; and **limited assurance**, conveying that nothing has come to the auditor’s attention to cause him/her to believe that the subject matter is not compliant with the criteria. Both reasonable and limited assurances are possible in both direct reporting and attestation engagements in compliance auditing.

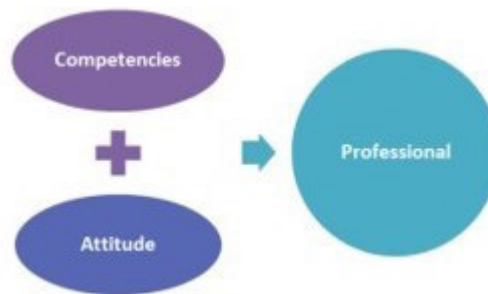
3.3.7 Principles of Compliance Auditing (Paragraph #42 et seq.)

General Principles

Auditors should plan and conduct the audit with professional scepticism and exercise professional judgement throughout the audit process.

The terms “professional scepticism” and “professional judgement” are relevant when formulating requirements regarding the auditor’s decisions about the appropriate course of action. They express the attitude of the auditor, which must include a questioning mind.

Figure 6: Professional Judgement and Scepticism



The auditor must apply professional judgement at all stages of the audit process. The concept refers to the application of relevant training, knowledge and experience, within the context provided by auditing standards, so that informed decisions can be made about the courses of action that are appropriate given the circumstances of the audit.

The concept of professional scepticism is fundamental to all audits. The auditor should plan and conduct the audit with an attitude of professional scepticism, recognising that certain circumstances may cause the subject matter to diverge from the criteria. An attitude of professional scepticism means the auditor making a critical assessment, with a questioning mind, of the sufficiency and appropriateness of evidence obtained throughout the audit.

Quality Control

Auditors should take responsibility for the overall quality of the audit.

The auditor is responsible for the performance of the audit and should implement quality control procedures throughout the audit process. Such procedures should be aimed at ensuring that the audit complies with the applicable standards and that the audit report, conclusion or opinion is appropriate given the circumstances.

Audit Team Management and Skills

Auditors should have access to the necessary skills.

The individuals in the audit team should collectively possess the knowledge, skills and expertise necessary to successfully complete the audit. This includes an understanding and practical experience of the type of audit being undertaken, familiarity with the applicable

standards and authorities, an understanding of the audited entity's operations and the ability and experience to exercise professional judgement. Common to all audits is the need to recruit personnel with suitable qualifications, offer staff development and training, prepare manuals and other written guidance and instructions concerning the conduct of audits, and assign sufficient audit resources. Auditors should maintain their professional competence through ongoing professional development.

Audits may require specialised techniques, methods or skills from disciplines not available within the SAI. External experts may be used in different ways, e.g. to provide knowledge or conduct specific work. Auditors should evaluate whether experts have the necessary competence, capabilities and objectivity and determine whether their work is adequate for the purposes of the audit.

Audit Risk

Auditors should consider audit risk throughout the audit process.

Audits should be conducted in such a way as to manage or reduce the audit risk to an acceptable level. The audit risk is the risk that the audit report – or more specifically the auditor's conclusion or opinion -will be inappropriate in the circumstances of the audit.

Consideration of audit risk is relevant in both attestation and direct engagements. The auditor should consider three different dimensions of audit risk – inherent risk, control risk and detection risk – in relation to the subject matter and the reporting format, i.e. whether the subject matter is quantitative or qualitative and whether the audit report is to include an opinion or a conclusion. The relative significance of these dimensions of audit risk depends on the nature of the subject matter, whether the audit is to provide reasonable or limited assurance and whether it is a direct reporting or an attestation engagement.

Table 4: Audit Procedures in Response to Inherent Risk

Inherent risk	Risk response	Audit approach
High	Low levels of controls	Audit response to be focused on improving internal controls through assessment of improved plans
High	Controls are asserted by the management to be adequate	Focus on obtaining assurance that controls continue to operate as designed and that there is consistency in risk management
Low	Low level of controls that may be consciously accepted by management	Evaluate and monitor the development of risk level
Low	High level of control	Audit response to be focused on compliance issues
<p>If the auditor identifies risks of material non-compliance the auditor should develop an overall response to such risks.</p> <p>The auditor should design further audit procedures, including tests of details (which may include tests of transactions) to obtain sufficient appropriate audit evidence about the entity's compliance with each of the applicable compliance requirements in response to the assessed risks of material noncompliance.</p>		

Materiality

Auditors should consider materiality throughout the audit process.

Determining materiality is a matter of professional judgement and depends on the auditor's

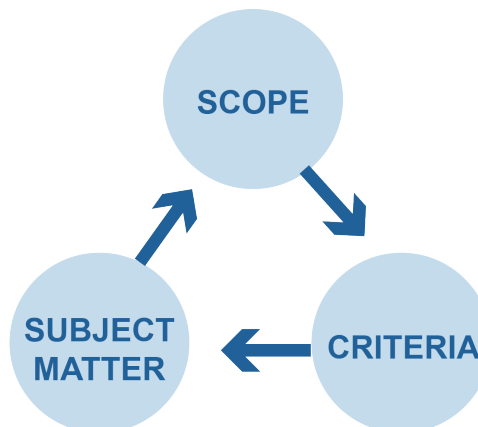
interpretation of the users' needs. A matter can be judged material if knowledge of it would be likely to influence the decisions of the intended users. This judgement may relate to an individual item or to a group of items taken together. Materiality is often considered in terms of value, but it also has other quantitative as well as qualitative aspects. The inherent characteristics of an item or group of items may render a matter material by its very nature. A matter may also be material because of the context in which it occurs.

Documentation

Auditors should prepare sufficient audit documentation.

Documentation should be prepared at the appropriate time and should provide a clear understanding of the criteria used, the scope of the audit, the judgments made, the evidence obtained and the conclusions reached. Documentation should be sufficiently detailed to enable an experienced auditor, with no prior knowledge of the audit, to understand the following: the relationship between the subject matter, the criteria, the audit scope, the risk assessment, the audit strategy and audit plan and the nature, timing, extent and results of the procedures performed; the evidence obtained in support of the auditor's conclusion or opinion; the reasoning behind all significant matters that required the exercise of professional judgement; and the related conclusions. The auditor should prepare relevant audit documentation before the audit report is issued, and the documentation should be retained for an appropriate period of time.

Figure 7: Relations Between Subject Matter, Scope and Criteria



Communication

Auditors should maintain effective communication throughout the audit process.

Communication takes place at all audit stages; before the audit starts, during initial planning, during the audit proper, and at the reporting phase. Any significant difficulties encountered during the audit, as well as instances of material non-compliance, should be communicated to the appropriate level of management or those charged with governance. The auditor should also inform the responsible party of the audit criteria.

3.3.8 Principles Related to the Audit Process: Planning and Designing a Compliance Audit

Audit Scope (Paragraph #50 et seq.)

Auditors should determine the audit scope.

Where the SAI's mandate or the applicable legislation does not prescribe the scope of the audit, this should be decided by the auditor. The audit scope is a clear statement of the focus, extent and limits of the audit in terms of the subject matter's compliance with the criteria. The scoping of an audit is influenced by materiality and risk, and it determines which authorities and parts thereof will be covered. The audit process as a whole should be designed to cover the entire audit scope.

Subject Matter and Criteria

Auditors should identify the subject matter and suitable criteria.

Determination of the subject matter and criteria is one of the first steps in a compliance audit.

The subject matter and criteria may be laid down by law or in the mandate of the SAI.

Alternatively, it may be identified by the auditor. For attestation engagements it may also be relevant to identify the subject matter information presented by the responsible party concerning the compliance of a given subject matter with certain criteria.

Understanding the Entity

Auditors should understand the audited entity in the light of the relevant authorities.

Compliance auditing may cover all levels of the executive and can include various administrative levels, types of entities and combinations of entities. The auditor should therefore be familiar with the structure and operations of the audited entity and its procedures for achieving compliance. The auditor will use this knowledge to determine materiality and assess the risk of non-compliance.

Understanding Internal Controls and the Control Environment

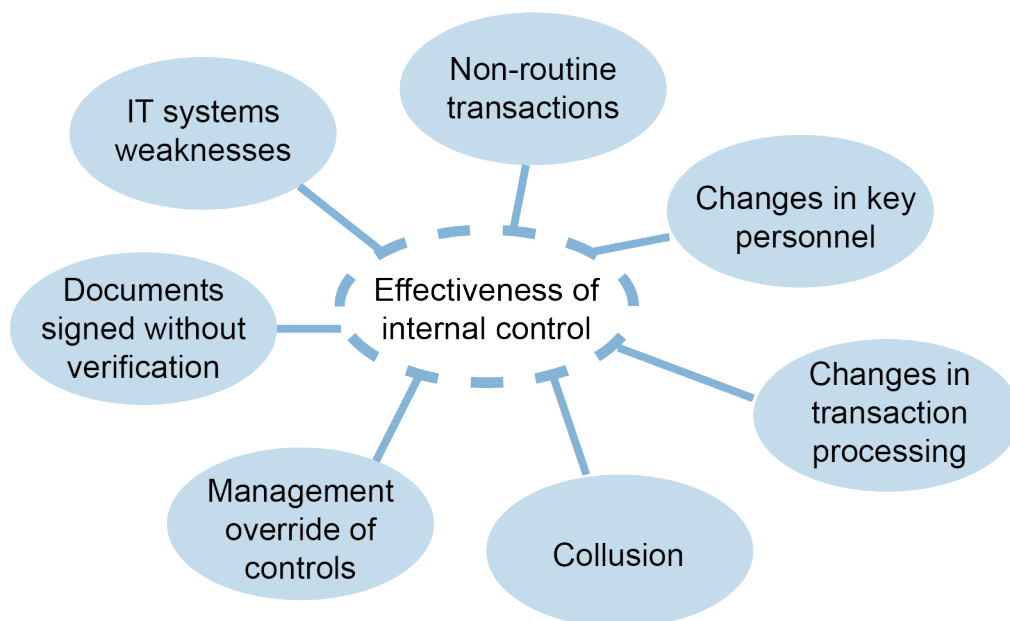
Auditors should understand the control environment and the relevant internal controls and consider whether they are likely to ensure compliance.

An understanding of the audited entity and/or the subject matter relevant to the audit scope depends on the auditor's knowledge of the control environment. The control environment is the culture of honesty and ethical behaviour that provides the foundation for the system of internal controls to ensure compliance with the authorities. In compliance auditing, a control environment that focuses on achieving compliance is of particular importance.

Table 5: Internal Control Components

CONTROL COMPONENT	PURPOSES
Control environment	To provide for the fundamental organisational structure, discipline and values of the entity. This creates an appropriate framework to ensure good governance of the resources entrusted.
Risk assessment	To identify and analyse internal and external risks to the achievement of the entity's objectives. In the Commission, all activities must have objectives that are intended to be specific, measurable, achievable, relevant and timely (SMART), as well as risk analysis and risk management of the main activities
Control activities	To define the policies and specific procedures implemented by the entity to ensure that the identified risks are appropriately managed. They include a range of activities as diverse as authorisations, verifications, reviews of operating performance, information processing, physical controls and segregation of duties. Control activities include controls over related party relationships and transactions.
Information & communication	To ensure an appropriate framework for achieving the financial reporting and compliance objectives; it includes the accounting system, procedures and records to initiate, record, process and report transactions and to maintain accountability for the related assets, liabilities and equity.
Monitoring	To ensure ongoing assessment of performance. This includes internal audit and evaluation, as well as the annual review of internal control.

Source: ECA Financial and Compliance Auditing Manual

Figure 8: Limitations on the Effectiveness of Internal Controls

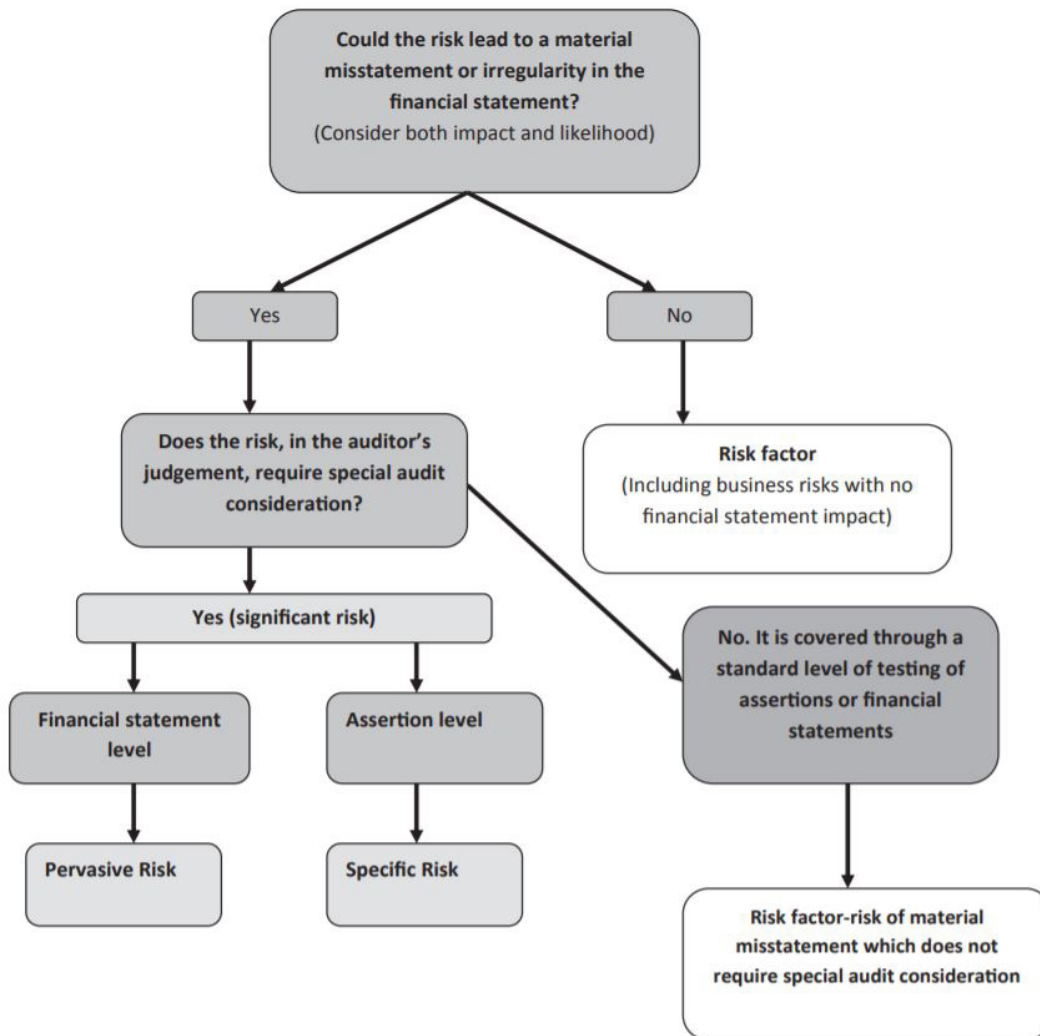
Source: Based on a figure from ECA Financial and Compliance Auditing Manual

Risk Assessment

Auditors should perform a risk assessment to identify risks of non-compliance.

In the light of the audit criteria, the audit scope and the characteristics of the audited entity, the auditor should perform a risk assessment to determine the nature, timing and extent of the audit procedures to be performed. In this the auditor should consider the risks that the subject matter will not comply with the criteria. Non-compliance may arise due to fraud, error, the inherent nature of the subject matter and/or the circumstances of the audit. The identification of risks of non-compliance and their potential impact on the audit procedures should be considered throughout the audit process. As part of the risk assessment, the auditor should evaluate any known instances of non-compliance in order to determine whether they are material.

Figure 9: Classification of Potential Risks



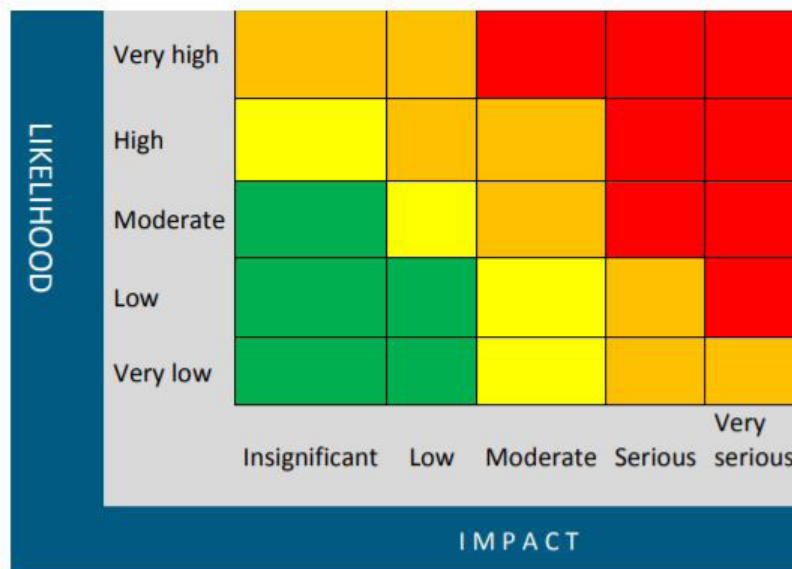
Source: Bangladesh Financial and Compliance Audit Manual

In the process of risk assessment, it is useful to apply a risk chart to place the risks in the right category as following:



You need to ask what is the likelihood that there is a risk of non-compliance of xyz requirements and what would be the impact if that risk occurs. Asking these questions related to the risks of non-compliance in a subject matter would help you to see a clear picture of the risks that are critical or high and in this manner, help you to prioritise if the risks are significant and whether you should persuade the subject matter further and conduct a compliance audit. Figure 10 provides an example of an Audit Risk Matrix.

Figure 10: Audit Risk Matrix



Source: AFROSAI-E Draft Compliance Audit Manual

Risk of Fraud

Auditors should consider the risk of fraud.

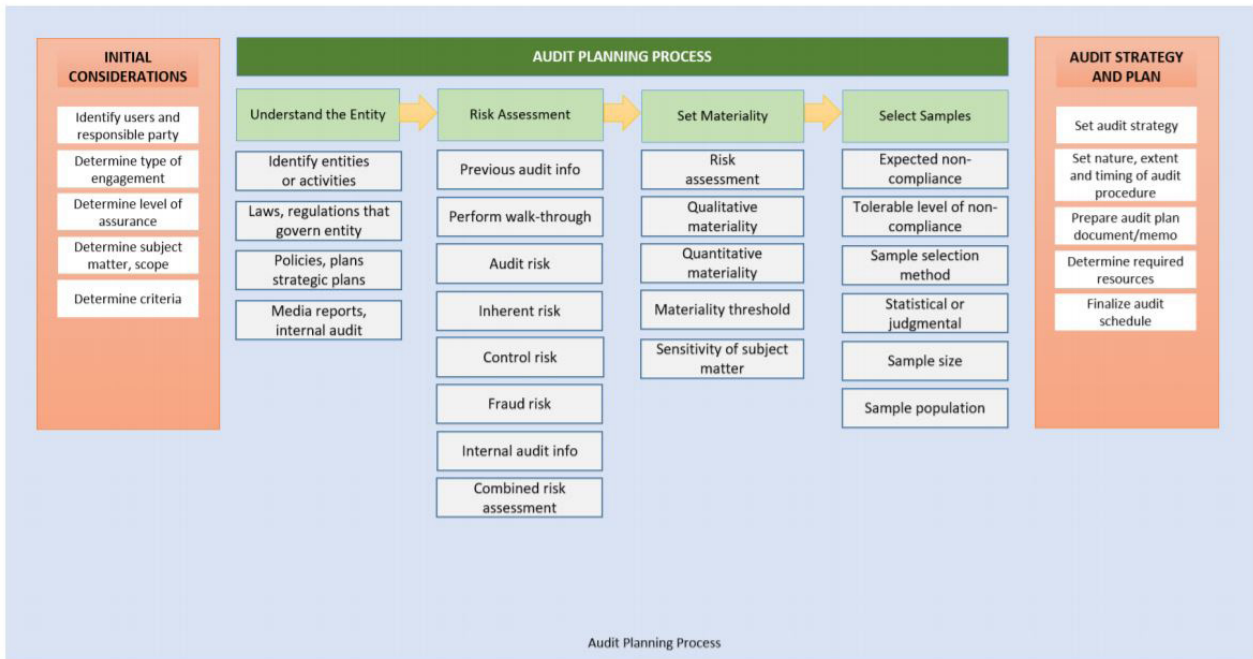
If the auditor comes across instances of non-compliance which may be indicative of fraud, he or she should exercise due professional care and caution so as not to interfere with any future legal proceedings or investigations.

Audit Strategy and Audit Plan

Auditors should develop an audit strategy and an audit plan.

Audit planning should involve discussion between members of the audit team with a view to developing an overall audit strategy and an audit plan. The purpose of the audit strategy is to devise an effective response to the risk of non-compliance. It should include consideration of the planned audit responses to specific risks through the development of an audit plan. Both the audit strategy and the audit plan should be documented in writing. Planning is not a distinct phase of the audit, but a continuous and iterative process.

Figure 11: The Audit Planning Process

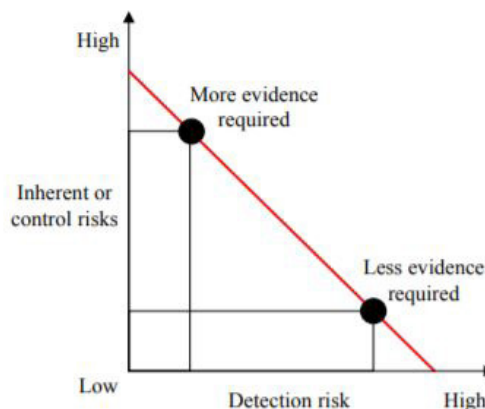


Source: IDI ISSAI Handbook Audit Evidence

Auditors should gather sufficient appropriate audit evidence to cover the audit scope.

The auditor should gather sufficient and appropriate audit evidence to provide the basis for the conclusion or opinion. **Sufficiency** is a measure of the quantity of evidence, while **appropriateness** relates to the quality of evidence – its relevance, validity and reliability. The quantity of evidence required depends on the audit risk (the greater the risk, the more evidence is likely to be required) and on the quality of such evidence (the higher the quality, the less may be required). Accordingly, the sufficiency and appropriateness of evidence are interrelated.

Figure 12: Relationship between Audit Evidence and Audit Risk



Source: ECA Financial and Compliance Manual

However, merely obtaining more evidence does not compensate for its poor quality. The reliability of evidence is influenced by its source and nature and is dependent on the specific circumstances in which it was obtained. The auditor should consider both the relevance and the reliability of the information to be used as audit evidence and must respect the confidentiality of all audit evidence and information received.

Evaluating Audit Evidence and Forming Conclusions

Auditors should evaluate whether sufficient and appropriate audit evidence has been obtained and form relevant conclusions.

After completing the audit proper the auditor will review the audit evidence in order to reach a conclusion or issue an opinion. The auditor should evaluate whether the evidence obtained is sufficient and appropriate so as to reduce the audit risk to an acceptably low level. The evaluation process entails considering evidence that both supports and seems to contradict the audit report, conclusion or opinion on compliance or non-compliance. It also includes considerations of materiality. After evaluating whether the evidence is sufficient and appropriate given the assurance level of the audit, the auditor should consider how best to conclude in the light of the evidence.

Table 6: Sources of Audit Evidence

Source	Examples of evidence	Quality as evidence	Audit considerations
Internal	Information from databases, documents and records produced by the audited entity	Lower, due to potential bias	Accuracy and completeness of such information should be evaluated
External	Confirmations (from banks, etc.) Work of other auditors/experts	Higher	Independence of the third party
Auditor	Analysis, computation, enquiry, inspection and observation	Highest	Base information may have been produced internally

Source: ECA Financial and Compliance Manual

If audit evidence obtained from one source is inconsistent with that obtained from another, or if there are any doubts about the reliability of the information to be used as evidence, the auditor should determine what modifications or additions to the audit procedures would resolve the matter and consider the implications, if any, for other aspects of the audit.

After completing the audit, the auditor will review the audit documentation to determine whether the subject matter has been sufficiently and appropriately examined. The auditor should also determine whether the risk assessment and initial determination of materiality were appropriate in the light of the evidence collected, or whether they need to be revised.

Table 7: Sources of Audit Evidence

Audit procedures to obtain evidence	Considerations
<i>PHYSICAL</i>	
Direct inspection or observation of people, property or events	While usually the most persuasive evidence, the auditor must be aware that his/her presence may distort reality.
<i>DOCUMENTARY</i>	
Review of accounting documents and records, manuals, management representations	Useful information may not always be documented, necessitating the use of other approaches.
<i>ORAL</i>	
Enquiry or interviews of auditee staff or third parties, documented or corroborated where possible.	Only on the rarest of occasions will the auditor accept information obtained in interviews to be reliable in its own right. (Reliability of audit evidence is greater if: obtained directly by the auditor rather than indirectly or by inference; received in documentary form rather than just orally,
<i>ANALYTICAL</i>	
Analysis through reasoning, reclassification, computation and comparison.	Such evidence is obtained by using professional judgment to evaluate physical, documentary and oral evidence.

Source: ECA Financial and Compliance Manual

Reporting

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.

Compliance audit reports should include the following elements (although not necessarily in this order):

1. Title
2. Addressee
3. Scope of the audit, including the time period covered
4. Identification or description of the subject matter
5. Identified criteria
6. Identification of the auditing standards applied in performing the work
7. A summary of the work performed
8. Findings
9. A conclusion/opinion
10. Replies from the audited entity (as appropriate)
11. Recommendations (as appropriate)
12. Report date
13. Signature

Follow-up

Auditors should follow up instances of non-compliance when appropriate.

A follow-up process facilitates the effective implementation of corrective action and provides useful feedback to the audited entity, the users of the audit report and the auditor (for future audit planning). The need to follow up previously reported instances of non-compliance will vary with the nature of the subject matter, the non-compliance identified and the particular circumstances of the audit. At some SAIs, including courts of accounts, the follow-up may include issuing legally binding reports or judicial decisions. In audits carried out on a regular basis the follow-up procedures may form part of the subsequent year's risk assessment.

3.4 Former Compliance Auditing Standards: ISSAI #4000 to #4300

Under the latest professional pronouncements, the previous four ISSAI (including a draft) have been replaced by a single standard **ISSAI #4000** (see [3.5](#)). The previous standards were:

- **ISSAI #4000:** which provided a brief general introduction;

- **ISSAI #4100:** deals with compliance audit performed separately from the audit of financial statements, for example as a separate audit task or related to performance audit;
- **ISSAI #4200:** deals with compliance audit related to the audit of financial statements; and
- **ISSAI #4300 (draft):** deals with compliance audits under the court model.

The three ISSAI (#4100; #4200 and #4300 (draft)) covered the different types of compliance auditing. They contained extensive examples of value to auditors and, although no longer standards, are important source documents for the auditor. To enable each to be a “standalone” document, much material was repeated between the three.

3.5 Compliance Auditing Standards: ISSAI #4000 to #4899

3.5.1 Introduction (Chapter #1 of ISSAI #4000; paragraphs 1 to 8)

Under the new ISSAI, there is now a single standard – **ISSAI #4000**.¹¹ The ISSAI 4000 contains mandatory requirements and explanations. Requirements contain the minimum necessary for high quality audit work. Requirements are “shall” statements presented in bold, while explanations elaborate the requirement in detail.

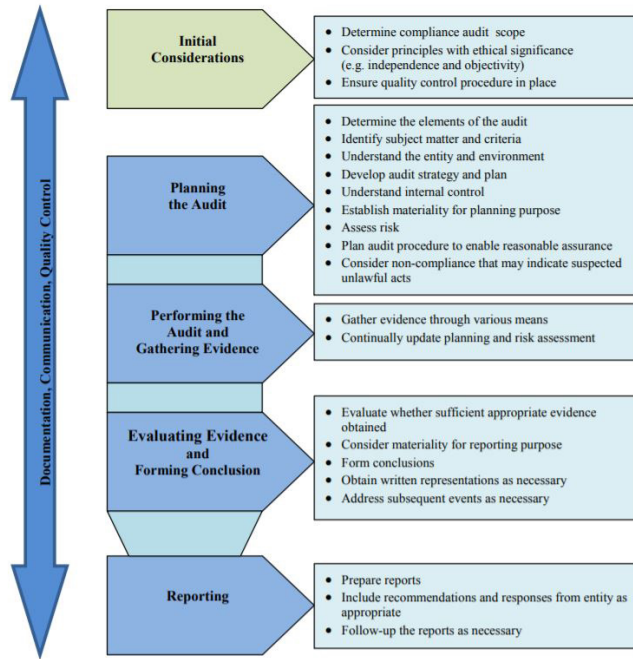
ISSAI #4000 is structured largely in the same order as ISSAI #400 and consists of four sections:

- The **first section** establishes the authority of the Compliance Audit Standards and how Supreme Audit Institutions (SAIs) can refer to them in their audit reports;
- The **second section** defines compliance auditing and its objectives, as well as the principles underlying the concept of compliance;
- The **third section** consists of general requirements for compliance auditing. These requirements shall be considered prior to commencement and throughout the audit process; and
- The **fourth section** contains requirements related to the main stages of the audit process itself.

As ever, this manual just highlights the main features of the standard and there is no substitute for reading the original document.

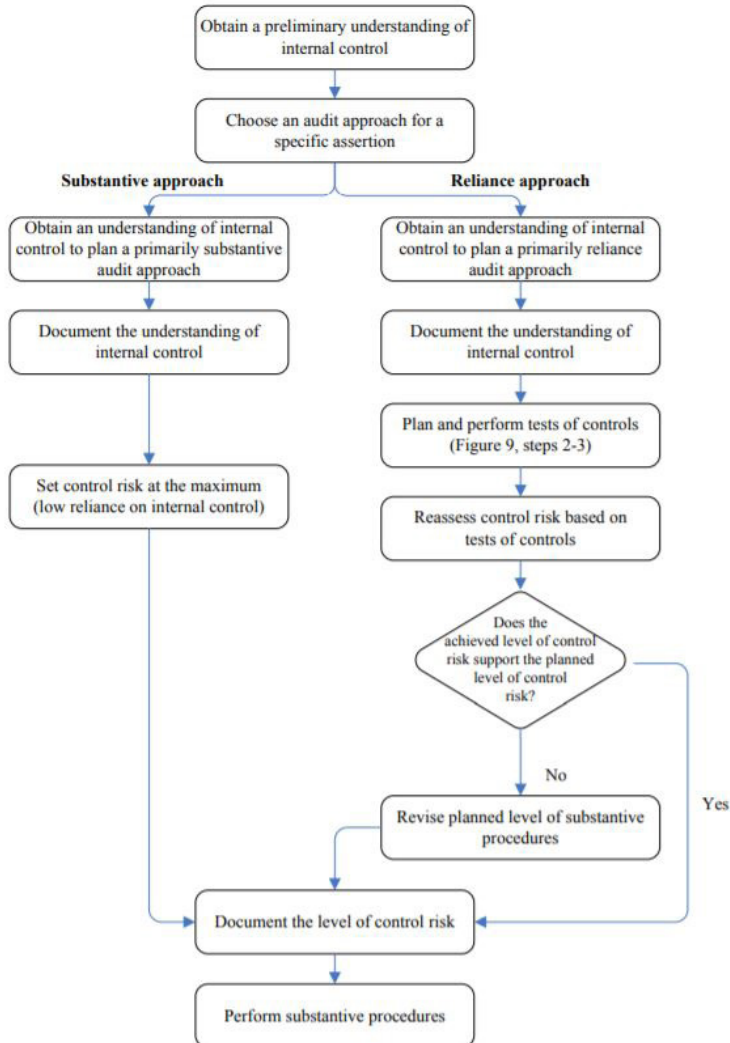
Figures 13 and 14 provide an overview of the Compliance Audit process and approach.

Figure 13: The Compliance Audit Process



Source: IDI ISSAI Handbook

Figure 14: Issues to Consider Regarding the Audit Approach



3.5.2 Scope (Chapter #2 of ISSAI #4000; paragraphs 9 to 18)

The ISSAI #4000 will in no way override national laws, regulations or mandates or prevent SAIs from carrying out investigations or other engagements that are not specifically covered.

This document provides the International Standard for Compliance Auditing. According to ISSAI #400/2–9, SAI wishing to make reference to the ISSAI framework relating to compliance auditing can do so in two ways:

- **Option 1:** by developing authoritative standards that are based on or consistent with the Compliance Audit Principles, or
- **Option 2:** by adopting the International Standards of Supreme Audit Institutions on Compliance Auditing (ISSAI #4000-4899).

Under **Option 1**, INTOSAI recognises that SAI have various mandates and work under different conditions. Due to the varied situations and structural arrangements of SAI, not all auditing standards or guidelines may apply to all aspects of their work. National standards can achieve the principles of ISSAI #400 in different ways, given the national mandate, constitutional and other legal environment or the strategy of the SAI.

SAI have the option of developing authoritative standards that are consistent with ISSAI #100 and ISSAI #400. If a SAI chooses to develop its own national standards, those standards should include the level of detail necessary to accomplish the SAI's relevant audit functions and should correspond to ISSAI #100 and ISSAI #400 in all applicable and relevant aspects.

SAI should declare which standard they apply when conducting audits and this declaration should be accessible to user(s) of the SAI's reports. SAI should make reference to the standard they follow in their audit reports; however, a more general form of communication may be used covering a defined range of engagements. Meaning that the SAI can state in their reports that they follow international standards without mentioning each individual standard used for each report. This is to make the reports more user friendly.

Under **Option 2**, the auditor and the SAI shall comply with each requirement of the ISSAI 4000, unless the requirement is not relevant. If all relevant requirements have not been fulfilled, reference to ISSAI #4000 shall not be made without disclosure of that fact and further explanations about the consequences thereof.

When a SAI chooses to make reference to ISSAI #4000, the reference should be formulated in accordance with the principles defined by ISSAI #100/10-12 and ISSAI 4#00/9. Compliance audits may be conducted either as a **stand-alone engagement** in accordance with ISSAI #4000 or **combined with financial or performance audit**.

For combined audits, the auditor assesses which standard to refer to. When a compliance audit is combined with a financial audit, the conclusion/opinion on the aspect of compliance should be clearly separated from the opinion on the financial statements. The identified applicable law(s) and regulation(s) should contain all laws and regulations that can influence the outcomes (=amounts) of the financial transactions that are (or should be) accounted for in the financial statements.

The requirements and explanations of ISSAI #4000 apply to compliance audits as a stand-alone engagement or a component of a financial or a performance audit engagement.

According to their mandate, SAI may also perform tasks that are not considered to be assurance engagements. These tasks are not covered by this ISSAI and therefore the SAI will have to refer to other standards or requirements for the work performed.

3.5.3 Three Parties in Compliance Auditing (Chapter #3 of ISSAI #4000; paragraph 19)

Public sector audits involve three separate parties: the responsible party, the auditor and the intended user(s).

- The responsible party is the executive branch of central or local government and/or its underlying hierarchy of public officials and entities responsible for the management of public funds and/or the exercise of authority under the control of the legislature. The responsible party in compliance auditing is responsible for the subject matter or the subject matter information of the audit;
- The auditor aims to obtain sufficient and appropriate audit evidence in order to arrive at a conclusion to enhance the degree of confidence of the intended user(s), other than the responsible party, about the measurement or evaluation of a subject matter against criteria; and
- The intended user(s) are the persons for whom the auditor prepares the compliance audit report. The intended user(s) may be legislative or oversight bodies, those charged with governance, the public prosecutor or the general public. While the audit report is not addressed to the responsible party, the result can be useful in the improvement of their performance.

3.5.4 Compliance Auditing Conducted by SAI with Jurisdictional Powers (Chapter #3 of ISSAI #4000; paragraphs 20 to 22)

SAI with jurisdictional powers have the authority to exercise judgment and make decisions concerning public officials responsible for non-compliant accounts. These SAIs have the authority to enforce sanctions. In doing so the SAIs comply with the basic principles of the rule of law. Some SAI are mandated to refer facts liable to criminal prosecution to the judicial authorities. For these SAI there may be national requirements in addition to the requirements in this ISSAI.

SAI with jurisdictional powers may also pronounce judgments and sanctions on those responsible for managing public funds and assets. Such SAI may assess whether responsible persons may be held liable for the loss, misuse or waste of public funds or assets and whether they ought to be subject to sanctions or penalties.

SAI with jurisdictional powers follow the audit process as it is described in these standards. However, following the planning, execution and evidence gathering phases, there may be additional and specific issues that may lead to legal proceedings and to a final formal judgment on the matters of noncompliance. Such issues are not covered by this ISSAI #4000.

3.5.5 Objectives of a Compliance Audit (Chapter #4 of ISSAI #4000; paragraphs 23 to 29)

The **main objective** of compliance auditing is to provide the intended user(s) with information on whether the audited public entities follow parliamentary decisions, laws, legislative acts, policy, established codes and agreed upon terms. These form the relevant authorities governing the subject matter/entity that is going to be audited. The authorities are the sources of audit criteria. The characteristics of the audit criteria are described below.

Compliance auditing includes both the aspects of regularity (adherence to formal criteria such as relevant laws, regulations and agreements) and/or propriety (observance of the general principles governing sound financial management and the conduct of public officials). Regardless of the source of criteria, the auditor performs the audit and forms a

conclusion with the selected level of assurance, in accordance with the requirements in ISSAI #4000.

The audit criteria might already be defined by the national legislation and/or the remit of the audited entity. In these cases, a SAI will not always have ability to influence the scope of the audit work.

The SAI promotes good governance by identifying and reporting deviations from criteria, so that corrective action may be taken and so that those responsible are held accountable for their actions. Compliance audits are carried out by assessing whether activities, financial transactions and information comply, in all material respects, with the authorities that govern the audited entity. Fraud is an intentional act of misrepresentation and is an element which counteracts transparency, accountability and good stewardship.

Compliance auditing is generally conducted either:

- As a separate compliance audit, or
- In relation with the audit of financial statements, or
- In combination with performance auditing.

The ISSAI #4000 does not provide detailed explanations on how to do combined audits.

An audit report provides important information as a base for decision making in the public sector. Audits provide this information based on sufficient and appropriate audit evidence. For each audit the needs of the intended user(s) are considered when deciding the level of assurance and hereby the level of sufficient and appropriate evidence. The auditor designs the audit to provide either a reasonable or a limited level of assurance.

3.5.6 Characteristics of a Compliance Audit (Chapter #4 of ISSAI #4000; paragraphs 30 to 32)

Every compliance audit is an **assurance engagement**. The auditor chooses the level of assurance based on the needs of the intended user(s). The audit report provides either reasonable or limited assurance.

Each assurance engagement is either an **attestation engagement or a direct reporting engagement**. Direct reporting engagement and attestation engagement differs based on who prepares and measure/evaluate the subject matter. The subject matter could either be set out in the mandate or selected by the SAI.

Regardless of the characteristics of the engagement, the audit criteria can include both regularity and propriety.

These standards are developed based on direct reporting audits but may be applied to assertion-based reporting as appropriate.

3.5.7 Reasonable and Limited Assurance (Chapter #4 of ISSAI #4000; paragraphs 33 to 36)

Reasonable assurance is high but not absolute. The audit conclusion is expressed positively, conveying that, in the auditor's opinion, the subject matter is or is not compliant in all material respects, or, where relevant, that the subject matter information provides a true and fair view, in accordance with the applicable criteria.

Normally a **reasonable assurance** audit report would require more audit evidence than a limited assurance, which often means more extended audit procedures, for example, in

matters of risk assessments, a better understanding of the entity environment, the evaluation of the design of the internal control system etc.

When providing **limited assurance**, the audit conclusion states that, based on the procedures performed, nothing has come to the auditor's attention to cause the auditor to believe that the subject matter is not in compliance with the applicable criteria. However, if the auditor believes that the subject matter is not in compliance with the criteria, s/he has to perform limited procedures to conclude whether the subject matter is in compliance with the criteria or not.

The procedures performed in a limited assurance audit are limited compared with what is necessary to obtain reasonable assurance, but the level of assurance is expected, in the auditor's professional judgment, to be meaningful to the intended user(s). A limited assurance report conveys the limited nature of the assurance provided.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4200 as they provide valuable additional information.

In most types of engagements there are two types of assurance levels: **reasonable (positive) assurance** and **limited (negative) assurance**.

Reasonable assurance is high, but not absolute assurance. Due to the inherent limitations of an audit (see section on risk assessment below), an audit does not normally provide 100% assurance. In general, reasonable assurance audits are designed to result in a positive form of expressing a conclusion, such as 'in our opinion the subject matter is / is not in compliance, in all material respects, with the stated criteria...'

Limited assurance work is not considered an audit, but rather a review-level engagement. It provides a lower level of assurance than an audit, and is designed to result in a negative form of expressing a conclusion, such as '*nothing has come to our attention that would indicate that the subject matter is not in compliance, in all material respects, with the criteria...*'

Both reasonable assurance audits and limited assurance reviews involve understanding the subject matter and obtaining sufficient appropriate evidence to support the public sector auditor's conclusion.

Reasonable assurance audits include assessing risks, performing audit procedures to respond to the assessed risks, and evaluating the sufficiency and appropriateness of the evidence obtained.

In performing a limited assurance review, procedures are usually limited to analytical procedures and inquiries. The nature, timing and extent of procedures performed in both reasonable assurance audits and limited assurance reviews are determined by public sector auditors applying professional judgement. A limited assurance review may be appropriate for subject matters across entities, which may involve more complex issues than subject matters within a specific entity.

These standards apply to auditing tasks where the purpose is to obtain sufficient appropriate evidence to support the findings. The conclusion may be expressed in a formalised statement of assurance or in a more elaborated form.

In some cases, management at the audited entity may prepare a specific assertion or a statement of compliance. In other instances, the assertion may be implicit. For example, in compliance audits performed as a separate audit task or together with performance audits, the assertion could be a statement of compliance with laws or regulations, a statement of

compliance with the terms of a contract, or a statement as to the effectiveness of a specific process or system.

An example of an implicit assertion may be when key performance indicators are subject to audit and they are presented on the inherent assumption that there has been no undisclosed noncompliance in achieving the levels of performance as set out in the key performance indicators.

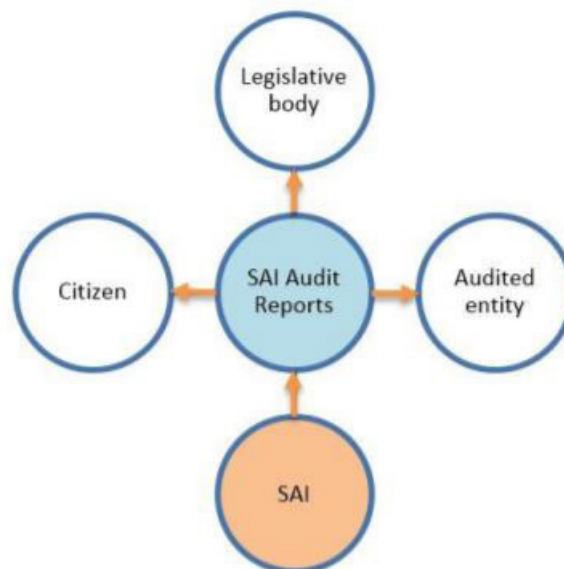
In many public sector audits, there are no specific assertions or statements of compliance that the audited entity makes available to users. Rather, the subject matter information is embedded in the auditor's report – either in the form of data/information or as an explicit statement in the form of a conclusion.

These types of audits are referred to as **direct reporting audits**. Audit findings are reported in an appropriate manner to relevant parties such as the audited entity and the legislature.

Reports are usually made available to the general public.

The form of reporting may vary depending on the auditor's professional judgement as to how to communicate most effectively with the intended users. Reports may be either short-form or long-form reports. More guidance on reporting is set out in the reporting section below.

Figure 15: Use of SAI Reports



3.5.8 Direct Reporting and Attestation Engagements (Chapter #4 of ISSAI #4000; paragraphs 37 to 42)

In a **direct reporting engagement**, it is the auditor who measures or evaluates the subject matter evidence against the criteria. The auditor is responsible for producing the subject matter information. The auditor selects the subject matter and criteria, taking into consideration risk and materiality. By measuring the subject matter evidence against the criteria, the auditor is able to form a conclusion. The conclusion is expressed in the form of findings, answers to specific audit questions, recommendations or an opinion.

In a direct reporting engagement performed with reasonable assurance, the audit conclusion expresses the auditor's view that the subject matter is or is not compliant in all material respects with the applicable criteria.

When providing limited assurance, the conclusion conveys that nothing has come to the auditor's attention that the findings are not in compliance with the audit criteria. When the auditor has been aware of instances of noncompliance, the conclusion needs to reflect this.

In an **attestation engagement** 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 forming a conclusion. The conclusion is expressed in the form of findings, conclusions, recommendations or an opinion.

In an attestation engagement with reasonable assurance the auditor's conclusion expresses the auditor's view that the subject matter information is/is not in accordance with the applicable criteria.

In an attestation engagement with limited assurance the auditor states whether or not, based on the procedures performed, anything has come to her/his attention to cause the auditor to believe that the subject matter is not in compliance, in all material respects, with the applicable criteria. The procedures performed are limited compared with what is necessary to obtain reasonable assurance.

3.5.9 Identification of Subject Matter and Scope (Chapter #4 of ISSAI #4000; paragraphs 43 to 44)

Some SAI have mandated requirements or have to perform audits on request from the Parliament, while other SAI have discretion to select the coverage of compliance audits. The way in which the subject matter is selected, has an impact on the audit approach when it comes to audit evidence and resources.

The scope defines the subject matter, and what is going to be audited. The scope depends on the needs of the intended user(s), the decided level of assurance, the risk that has been assessed and the competence and resources available in the SAI.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

The determination of the **subject matter** and the **subject matter information** is one of the first steps to be carried out in planning and performing a compliance audit.

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.

In some cases, the subject matter may be set out in the relevant law or audit mandate.

In other cases the selection of the subject matter is a strategic choice to be made by the SAI or public sector auditors, and is based on risk assessment and professional judgement.

When compliance audit encompasses budgetary laws, or other relevant budgetary resolutions, the entity's revenue and financing are included, as well as its expenditure.

A SAI's mandate may also encompass audits of compliance with the documented budgetary

assumptions and premises, prior to the applicable resolution of the legislature.

When performed in connection with an audit of financial statements, the subject matter of a compliance audit is generally decisions and financial management in relation to the use of appropriated funds and execution of the budget. Such a compliance audit comprises the assessment of whether the activities, financial transactions and information reflected in the financial statements (the subject matter information) are in accordance with the authorities which govern them (the criteria).

Such authorities may include the applicable law, including budgetary law in particular, basic principles of law, legislative acts, parliamentary decisions, and other authoritative decisions, directions and guidelines, and agreed upon terms and conditions. Whether the entity's income and expenditure have been applied to the purposes intended by the legislature, and to the entity's mandated program objectives and activities is generally also encompassed.

Some examples of subject matters and subject matter information in relation to compliance auditing are set out in [Annex 4](#).

3.5.10 Objectivity and Ethics (Chapter #5 of ISSAI #4000; paragraphs 45 to 51)

To avoid excessive quotations from the standard, this section of the manual will only detail the **Audit Requirements**. However, additional explanation is provided when considered relevant. The original bolding of the requirements has been retained.

The auditor shall comply with the relevant procedures relating to objectivity and ethics, which in turn shall comply with the related ISSAIs on objectivity and ethics.

The auditor shall take care to remain objective so that findings and conclusions will be impartial and shall be seen as such by third parties.

3.5.11 Audit Risk (Chapter #5 of ISSAI #4000; paragraphs 52 to 57)

The auditor shall perform procedures to reduce the risk of producing incorrect conclusions to an acceptable low level.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

Risk assessment is an essential part of performing a reasonable assurance audit. Due to the inherent limitations of an audit, a compliance audit does not provide a guarantee or absolute assurance that all instances of non-compliance will be detected.

Inherent limitations in a compliance audit may include factors such as:

- a) Judgement may be applied by management in interpreting laws and regulations;
- b) Human errors occur;
- c) Systems may be improperly designed or function ineffectively;
- d) Controls may be circumvented; and
- e) Evidence may be concealed or withheld.

In performing compliance audits, public sector auditors assess risk and perform audit procedures as necessary throughout the audit. This is done in order to reduce audit risk to an acceptably low level in the particular circumstances, so as to obtain reasonable

assurance as the basis for the auditor's conclusion.

The risks and the factors that may give rise to such risks will vary depending on the particular subject matter and circumstances of the audit. In general, public sector auditors consider the three elements of audit risk - inherent risk, control risk and detection risk in relation to the subject matter and the particular situation. In addition, the probability that the matter will occur, and the possible consequences arising if the matter should occur, are also taken into account in assessing risk.

Relationships between various public sector entities are considered when assessing audit risk, and especially when assessing the risk of fraud or non-compliance. Such risks may, for example, relate to one entity exerting influence over another entity to take inappropriate actions. The result of these actions may be non-compliance with authorities, and in some cases the result may be an unlawful act. Furthermore, in the public sector there may be specific requirements related to activities and transactions between various public sector entities. There may also be specific reporting requirements related to such activities or transactions that may impact the planned audit procedures, the audit opinion or the auditor's report.

Examples of factors related to assessing risk in compliance audits are set out in [Annex 7](#).

3.5.12 Risk of Fraud (Chapter #5 of ISSAI #4000; paragraphs 58 to 63)

The auditor shall consider the risk of fraud throughout the audit process, and document the result of the assessment.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

As part of the audit, public sector auditors identify and assess fraud risk and gather sufficient appropriate evidence related to identified fraud risks through the performance of suitable audit procedures. When suspected fraud has been identified, public sector auditors take action to ensure that they respond appropriately based upon the mandate of the SAI and the particular circumstances.

Fraud risks and assessments of materiality in relation to fraud are considered in the context of the broader scope of public sector auditing. Examples of areas and situations that may typically give rise to fraud risks in the public sector include:

- a) Grants and benefits to third parties;
- b) Procurement;
- c) Exercise of public officials' duties and power;
- d) Intentional misstatement or misrepresentation of results or information;
- e) Privatisation of government entities; and
- f) Relationships between public sector officials or entities.

3.5.13 Selection of Areas of Significance for the Intended User(s) (Chapter #5 of ISSAI #4000; paragraphs 64 to 70)

Where the SAI has discretion to select the coverage of compliance audits it shall identify areas that are of significance for the intended user(s).

3.5.14 Professional Judgement and Scepticism (Chapter #5 of ISSAI #4000; paragraphs 71 to 79)

The auditor shall exercise professional judgment throughout the audit process.

If expertise in a difficult or contentious issue is not available in the audit team, professional advice shall be sought.

The auditor shall exercise professional scepticism and maintain an open and objective mind.

3.5.15 Quality Control (Chapter #5 of ISSAI #4000; paragraphs 80 to 88)

The SAI shall take responsibility for the overall quality of the audit to ensure that the audits are carried out in accordance with relevant professional standards, laws and regulations, and that the reports are appropriate in the circumstances.

The SAI shall ensure that the audit team collectively has the necessary professional competence to perform the audit.

3.5.16 Documentation (Chapter #5 of ISSAI #4000; paragraphs 89 to 95)

The auditor shall prepare audit documentation that is sufficiently detailed to provide a clear understanding of the work performed, evidence obtained and conclusions reached. The auditor shall prepare the audit documentation in a timely manner, keep it up to date throughout the audit, and complete the documentation of the evidence supporting the audit findings before the audit report is issued.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

The Fundamental Auditing Principles state that audit evidence gathered must be adequately documented (ISSAI #300, 3.5.5 and 3.5.6). Documentation in regard to compliance audits includes documenting sufficiently matters that are significant in providing evidence to support the conclusions drawn and the report issued.

The audit documentation should be sufficiently complete and detailed to enable an experienced auditor, having no previous connection with the audit, to understand what work was performed in support of the conclusions (ISSAI #300, 3.5.7).

Documentation takes place throughout the entire audit process. Public sector auditors prepare compliance audit documentation on a timely basis, and maintain such documentation which records the criteria used, the work done, evidence obtained, judgements made and review performed. Public sector auditors prepare relevant audit documentation before the auditor's report is issued. Audit documentation is retained for an appropriate period of time.

3.5.17 Communication (Chapter #5 of ISSAI #4000; paragraphs 96 to 100)

The auditor shall communicate in an effective manner with the audited entity and those charged with governance throughout the audit process.

Instances of material non-compliance shall be communicated with the appropriate level of management and (if applicable) those charged with governance. Other significant matters arising from the audit that are directly relevant to the entity shall also be communicated.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

Good communication with the audited entity throughout the audit process may help make the process more effective and constructive. Communication takes place at various phases and at various levels, for example:

- a) During the **initial planning phase**, including discussing with the appropriate level of management, and those charged with governance as appropriate - within the limits of laws and regulations - the audit strategy, timing, logistics, responsibilities, suitable audit criteria and other elements of planning;
- b) During the **performance phase** and throughout the audit, including gathering evidence and making inquiries of relevant persons as appropriate. Any significant difficulties encountered during the audit, as well as instances of material non-compliance are promptly communicated to the appropriate level of management, or to those charged with governance. Other less significant findings that are not deemed material, or do not warrant inclusion in the public sector auditor's report, may also be communicated to management during the audit. Communicating such less significant findings may also help the audited entity to remedy instances of non-compliance and avoid similar instances in the future. For this reason, many public sector auditors communicate all identified instances of non-compliance to management; and
- c) During the **reporting phase**, including issuing written reports on a timely basis to the intended users, the audited entity and others as appropriate.

Some SAI can, according to their audit mandate, order the audited entity to correct identified instances of non-compliance. In doing so, public sector auditors determine whether their independence and objectivity will be impaired and take appropriate action to avoid such impairment.

3.5.18 Identifying Intended User(s) and Responsible Parties (Chapter #6 of ISSAI #4000; paragraphs 101 to 106)

The auditor shall explicitly identify the intended user(s) and the responsible party and consider the implication of their roles in order to conduct the audit and communicate accordingly.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

Public sector auditors ensure that the necessary preconditions exist in order to effectively perform the audit. In planning compliance audits, this may involve identifying at the outset the relevant parties involved. This is important in order to establish the legal basis for performing the audit, such as the mandate of the SAI, including the responsibilities of public sector auditors, and the constitutional status and responsibilities of the audited entity.

In addition, it is important to identify the users of the audit report. The form and content of the report are influenced by the auditor's professional judgement as to how to communicate most effectively with the intended users. The needs of users may vary depending upon whether the users are the legislature, a funding agency, a donor organisation, the citizens or other relevant stakeholders.

3.5.19 Defining the Subject Matter and Corresponding Audit Criteria (Chapter #6 of ISSAI #4000; paragraphs 107 to 120)

Where the SAI has discretion to select the coverage of compliance audits, the auditor shall define the subject matter to be measured or evaluated against criteria.

Where the SAI has discretion to select the coverage of compliance audits, the auditor shall identify relevant audit criteria prior to the audit to provide a basis for a conclusion/an opinion on the subject matter.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

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 [Annex 4](#).

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.

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 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; and

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.

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.

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 [Annex 5](#).

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.

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.

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.

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).

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.

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.

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.

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

The audit approach may also be broken down into parts, or the scope narrowed, such that clearly identifiable criteria may be applied.

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.

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.

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 [Annex 6](#).

3.5.20 Determining the Level of Assurance (Chapter #6 of ISSAI #4000; paragraphs 121 to 124)

Depending on the mandate of the SAI, the characteristics of the subject matter, and the needs of the intended user(s), the auditor shall decide whether the audit shall provide reasonable or limited assurance.

3.5.21 Determining Materiality (Chapter #6 of ISSAI #4000; paragraphs 125 to 130)

The auditor shall determine materiality to form a basis for the design of the audit and re-assess it throughout the audit process.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

Materiality consists of both quantitative and qualitative factors. In performing compliance

audits, materiality is determined for:

- a) Planning purposes;
- b) Purposes of evaluating the evidence obtained and the effects of identified instances of non-compliance; and
- c) Purposes of reporting the results of the audit work.

Public sector auditors plan and perform the audit to determine whether the subject matter information, in all material respects, is in compliance with the stated criteria.

As stated in the Fundamental Auditing Principles:

“Materiality is often considered in terms of value but the inherent nature or characteristics of an item or group of items may also render a matter material—for example, where the law or regulation requires it to be disclosed separately regardless of the amount involved.” (ISSAI 100, 1.0.10)”

During the planning process, information is gathered about the entity in order to assess risk and establish materiality levels for designing audit procedures. Evidence gathered must then be evaluated as a basis for forming conclusions and for reporting purposes. Materiality is significant to this evaluation.

The determination of materiality for planning purposes may be straight forward. This might be the case in situations where a law or regulation or agreed-upon terms establish an unconditional requirement for compliance, for example if the constitution prohibits overspending in relation to the approved budget.

Other matters that may be considered material at a lower level of value or incidence than the general determination of materiality include:

- a) Fraud;
- b) Intentional unlawful acts or non-compliance;
- c) Incorrect or incomplete information to management, the auditor or to the legislature (concealment);
- d) Intentional disregard for follow-up of requests made by management, authoritative bodies or auditors; and
- e) Events and transactions made despite knowledge of the lack of legal basis to carry out the particular event or transaction.

In other cases, the determination of materiality is normally a matter for professional judgement.

When evaluating evidence obtained, the determination of materiality may be influenced by quantitative factors such as the number of persons or entities affected by the particular subject matter, or the monetary amounts involved. In some cases, the qualitative factors are more important than the quantitative factors.

The nature, visibility and sensitivity of the particular programme area or subject matter may play a role. For example, the emphasis placed on the subject matter by users, a public accounts committee or similar committee of the legislature, or regulatory bodies may influence the determination of materiality.

Public expectations and public interest are also qualitative factors that may impact the

public sector auditor's determination of materiality. The seriousness of the non-compliance is also considered. While not necessarily unlawful, instances of excess spending over appropriations authorised by the legislature or introduction of a new service not provided for in the approved appropriations may be serious instances of non-compliance by their nature.

In evaluating the materiality of any non-compliance identified, matters such as the criteria, the conditions, the cause and the effect of non-compliance are also considered.

3.5.22 Understanding the Entity and its Environment including Internal Control (Chapter #6 of ISSAI #4000; paragraphs 131 to 136)

The auditor shall have an understanding of the audited entity and its environment, including the entity's internal control, to enable effective planning and execution of audit.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

Determining the subject matter and suitable criteria as explained above are among the first steps in performing compliance audits. The process of determining the subject matter and the criteria involves public sector auditors obtaining **an understanding of the audited entity and the circumstances surrounding the audit.**

This understanding provides public sector auditors with a frame of reference to be used in applying professional judgement throughout the entire auditing process. An understanding of the entity, its environment and relevant program areas is especially important as it will be used in determining materiality and in assessing risks. Some examples of sources that may be used in gaining this understanding are set out in [Annex 5](#).

Understanding internal control is normally an integral part of understanding the entity and the relevant subject matter. The Fundamental Auditing Principles explain that in performing an audit, public sector auditors understand and evaluate the reliability of internal control (ISSAI #300, 3.3.1). In compliance audit, this includes understanding and evaluating controls that assist management in complying with laws and regulations (ISSAI #300, 3.3.2).

The particular type of controls evaluated depends on the subject matter, and the nature and scope of the particular compliance audit. In evaluating internal control, public sector auditors assess the risk that the control structure may not prevent or detect material non-compliance (ISSAI #300, 3.4.6). The internal control system in an entity may also include controls designed to correct identified instances of non-compliance.

Public sector auditors obtain an understanding of internal control relevant to the audit objective, and test controls on which they expect to rely. The assurance derived from the assessment of the internal controls will help the auditors determine the confidence level and hence, the extent of the audit procedures to perform.

3.5.23 Audit Strategy and Audit Plan (Chapter #6 of ISSAI #4000; paragraphs 137 to 143)

The auditor shall develop and document an audit strategy and an audit plan that together describe how the audit will be performed to issue reports that will be appropriate in the circumstances, the resources needed to do so and the time schedule for the audit work.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

Planning audit procedures involves designing procedures to respond to the identified risks of non-compliance. The exact nature, timing and extent of the audit procedures to be performed may vary widely from one audit to the next.

Nonetheless, compliance audit procedures in general involve establishing the relevant criteria, i.e. the authorities which govern the entity, and then measuring the relevant subject matter information against such authorities. The Fundamental Auditing Principles state that the auditor should plan the audit in a manner which ensures that an audit of high quality is carried out in an economic, efficient and effective way and in a timely manner (ISSAI #300 3.1.1). Furthermore, those planning the audit need to be knowledgeable of the compliance requirements that apply to the entity being audited (ISSAI #300, 3.4.3).

Public sector auditors plan and perform audits while maintaining an attitude of professional scepticism.

Planning the audit so that it will be performed effectively involves discussions with relevant members of the audit team and developing an overall audit strategy and an audit plan. Both the audit strategy and the audit plan should be documented in writing. Planning is not a distinct phase of the audit but is a continual and iterative process. The overall audit strategy and plan are updated as necessary throughout the audit. Planning also involves considerations related to the direction, supervision and review of the engagement team.

In establishing the overall audit strategy for the compliance audit, public sector auditors consider:

- a) The objectives, scope, subject matter, criteria and other characteristics of the compliance audit, taking into account the mandate of the SAI and the elements contained in the compliance audit definition;
- b) Reporting responsibilities and objectives, as well as to whom and when such reporting will take place, and in what form;
- c) Significant factors that may influence the direction of the audit;
- d) Materiality and audit risk assessment;
- e) Knowledge gained from previous or related audits;
- f) Composition and work allocation of the audit team, including any need for experts; and
- g) Timing of the audit.

Public sector auditors develop an audit plan for the compliance audit. The audit strategy is essential input to the audit plan. The audit plan includes:

- a) A description of identified criteria related to the scope and characteristics of the compliance audit and to the legal, regulatory or appropriations framework;
- b) A description of the nature, timing and extent of risk assessment procedures sufficient to assess the risks of non-compliance, related to the various audit criteria; and
- c) A description of the nature, timing and extent of planned audit procedures related to the various compliance audit criteria and risk assessments.

Planning also involves:

- a) Obtaining a general understanding of the legal, regulatory and appropriations framework, as well as relevant, agreed upon terms and conditions applicable to the scope of the audit and to the audited entity;
- b) Obtaining an understanding of management's assessment of applicable laws and regulations including management's internal controls that help ensure compliance with authorities;
- c) Obtaining an understanding of the relevant authorities, including rules, laws, regulations, policies, codes, significant contracts or grant agreements etc; and
- d) For audits of propriety – obtaining an understanding of relevant principles of sound public sector financial management and expectations regarding the conduct of public sector officials.

3.5.24 Sufficient and Appropriate Audit Evidence (Chapter #7 of ISSAI #4000; paragraphs 144 to 171)

The auditor shall plan and perform procedures to obtain sufficient and appropriate audit evidence to form a conclusion with the selected level of assurance.

The auditor in a SAI with jurisdictional powers shall perform procedures to obtain sufficient and appropriate audit evidence regarding the liability of the public official who might be held responsible for non-compliance/unlawful acts.

The auditor shall select a combination of audit techniques to be able to form a conclusion with the selected level of assurance.

In SAIs with jurisdictional powers, the inquiry shall be carried out in written form when requested by the national law.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

The Fundamental Auditing Principles state that public sector auditors choose and perform audit steps and procedures that, in their professional judgement, are appropriate in the circumstances. (ISSAI #300, 3.4.5). The Fundamental Auditing Principles also state that the steps and procedures are designed to **obtain sufficient, competent, and relevant evidence** that will provide a reasonable basis for the auditor's judgements and conclusions (ISSAI #300, 3.5.1).

Evaluating the entity's internal control systems and assessing the risks that the control systems may not prevent or detect instances of non-compliance are a normal part of performing compliance audits (ISSAI #300 3.4.6).

The audit procedures to be performed will depend on the particular subject matter and criteria identified, as well as the auditor's professional judgement. The procedures should be clearly linked to the identified risks. When the risks of noncompliance are significant and public sector auditors plan to rely on the controls in place, such controls must be tested. When controls are not considered reliable, public sector auditors plan and perform substantive procedures to respond to the identified risks. Furthermore, additional substantive procedures are performed when there are significant risks of non-compliance. If the audit approach consists only of substantive procedures, tests of details (not only analytical tests) are performed.

In some rare cases it may be difficult or almost prohibitively expensive to obtain sufficient, appropriate audit evidence in order to form conclusions. In these cases, public sector auditors must consider the relationship between the costs and the benefits of gathering the evidence, as well as the consequences lack of sufficient appropriate evidence will have on the achievement of the audit objectives and on the auditor's report. The auditor's response to this situation may vary in the circumstances depending on the mandate, public interest considerations, public expectations and the ability to report such findings. The auditor may find it necessary to report on this matter specifically to the legislature or other intended users.

However, such difficulty or expense is not, in itself, sufficient grounds for omitting the planned evidence-gathering procedures, even if there are no satisfactory alternative procedures.

Some examples of compliance audit procedures for selected subject matters are set out in [Annex 8](#).

Gathering and Evaluating Evidence

In performing a reasonable assurance audit, public sector auditors gather sufficient appropriate audit evidence to provide a basis for the auditors' conclusions. The Fundamental Auditing Principles state that:

“competent, relevant and reasonable evidence should be obtained to support the auditor's judgement and conclusions regarding the organisation, program, activity or function under audit” (ISSAI #300,3.5.1).

The sufficiency of evidence relates to the quantity of the evidence. The competence, relevance, reliability and appropriateness of evidence relates to the quality of the evidence. Public sector auditors exercise professional judgement in making the determination of sufficiency and appropriateness throughout the evidence gathering process.

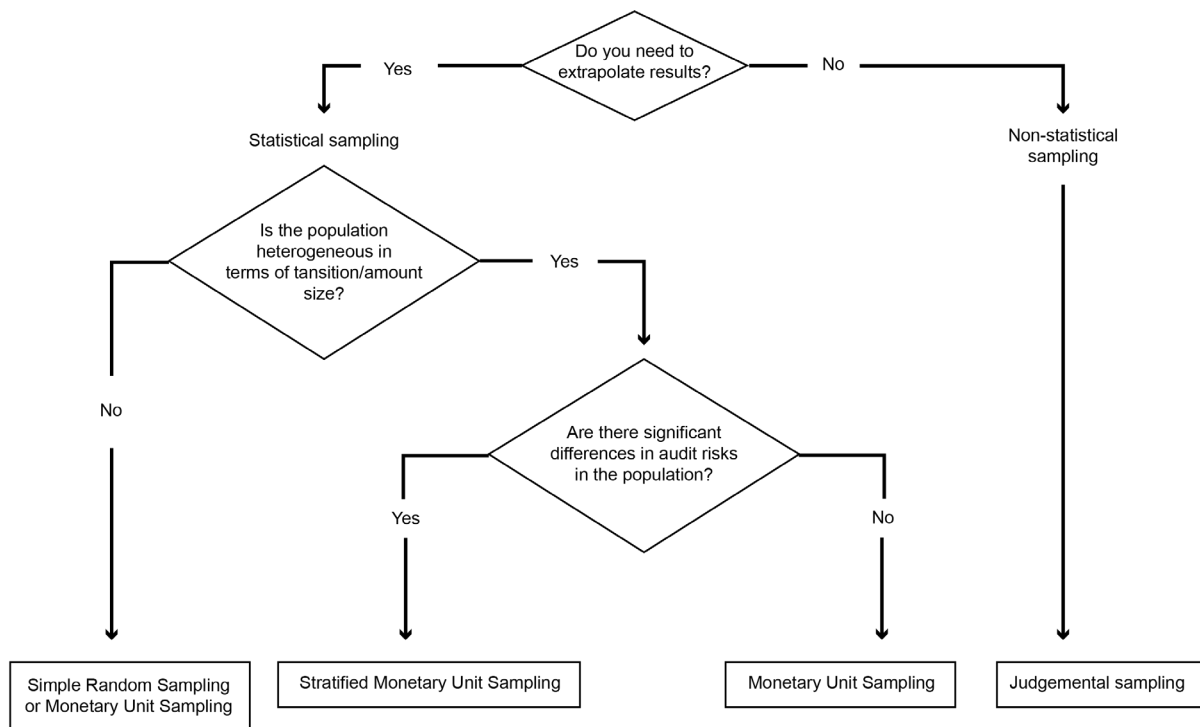
The evidence gathering process is systematic and iterative and involves:

- a) Gathering evidence by performing appropriate audit procedures;
- b) Evaluating the evidence obtained as to its sufficiency (quantity) and appropriateness (quality); and
- c) Re-assessing risk and gathering further evidence as necessary.

The evidence gathering process continues until the public sector auditor is satisfied that sufficient, appropriate evidence exists to provide a basis for the auditor's conclusion.

In many cases, audit sampling may be used as a means of testing to detect instances of non-compliance with authorities. The use of IT audit techniques is often helpful and in many cases is an integrated part of a compliance audit.

Figure 16: How to Determine Sampling Selection Method



Source: ICA Financial and Compliance Audit Manual

Audit evidence is gathered using a variety of techniques such as:

- a) Observation;
- b) Inspection;
- c) Inquiry;
- d) Re-performance;
- e) Confirmation; and
- f) Analytical procedures.

Procedures to gather audit evidence are generally grouped into two major categories:

- a) Tests of controls; and
- b) Substantive tests, such as analytical procedures or tests of details.

Observation

Observation involves looking at a process or procedure being performed. In performing compliance audit, this may include looking at how a bid tendering process is carried out or observing how benefit payments are processed.

Inspection

Inspection involves examining books, records and other case files or physical assets.

In performing compliance audit, inspection may include examining the books and records to determine how project funds have been accounted for and comparing the accounting to the terms of the project agreement. Inspection of case files may involve examining all relevant documents to determine if recipients of benefits met eligibility requirements. Inspection may also involve examining an asset, such as a bridge or a building, to determine if it meets the

applicable building specifications.

Public sector auditors consider the reliability of any documents inspected and keep in mind the risk of fraud and the possibility that documents inspected may not be authentic. In cases of fraud, sometimes two different sets of books and records have been kept. Public sector auditors may also inquire with different persons as to the source of the documents, or the controls over their preparation or maintenance.

Inquiry

Inquiry involves seeking information from relevant persons, both within and outside the audited entity. Inquiry may range from formal written inquiries to more informal oral discussions. It may involve interviewing and asking questions of relevant persons, including experts. Such interviews may take place in person or virtually (for example phone calls or web-meetings). Inquiry may also involve preparing and sending questionnaires or surveys.

Inquiry is generally used extensively throughout an audit and complements other audit procedures. For example, when observing processes being performed, such as the benefits payment process mentioned above, inquiries are often made of relevant persons in regard to how relevant legislation, including changes and updates, is identified and interpreted. Results of inquiries may indicate that the processes are performed in different ways in different locations, which may lead to instances of non-compliance.

Inquiries are often made of persons outside the particular function subject to audit.

For example, in addition to making inquiries of accounting personnel, it may also be relevant to make inquiries of legal or technical personnel.

Inquiry is generally not sufficient appropriate evidence on its own. In order to obtain sufficient appropriate evidence, inquiry is performed together with other types of procedures. Inquiry is most effective when conducted with relevant and knowledgeable persons, ie persons in positions of authority who are authorised to speak or give opinions on behalf of the entity.

Figure 17: Combination of Techniques for Evidence Gathering



Source: AFROSAI-E Draft Compliance Audit Manual

Confirmation

Confirmation is a type of inquiry and involves obtaining, independently from the audited entity, a reply from a third party in regard to some particular information. In compliance audits, confirmation may involve the auditor obtaining feedback directly from beneficiaries that they have received the grants or other funds that the audited entity asserts have been paid out, or confirming that funds have been used for the particular purpose set out in the

terms of a grant or funding agreement. Confirmation may also involve receiving guidance from the legislature as to how a specific piece of legislation is meant to be interpreted.

Written confirmations may also be obtained from management in regard to oral representations made during the audit. These written management representations may, for example, relate to:

- a) Management's assertion of compliance with a relevant piece of legislation, the terms of an agreement, etc.;
- b) Management's disclosure of all instances of non-compliance of which it is aware; and
- c) Management having provided the auditor with complete information about the subject matter.

Re-performance

Re-performance involves independently carrying out the same procedures already performed by the audited entity. Re-performance may be done manually or by computer assisted audit techniques. For example, case file studies may be performed to test whether the audited entity made the correct decisions or provided the appropriate service in accordance with the relevant criteria.

Process steps may be re-performed to test the appropriateness of visas or resident permits issued, or the exercise of budget authority. If the criteria for making child benefit payments involve payments to parents with children under a certain age, the audited entity's selection of recipients from a public database may be re-performed by public sector auditors using computer assisted audit techniques to test the accuracy of the entity's process.

Also, if the selection of bids from a tender process is dependent upon meeting certain criteria, the bid selection process may be re-performed to test that the correct bids have been selected. Where highly technical matters are involved (for example re-performance of pension calculations or engineering models), experts may be involved.

Analytical Procedures

Analytical procedures involve comparing data or investigating fluctuations or relationships that appear inconsistent. In compliance auditing, such procedures may, for example, involve comparing an increase in pension benefits payments from one year to the next with demographic information such as the number of citizens having reached retirement age within the last year. If the criteria relate to the terms of an agreement which state, for example, that project funding is provided based on performance levels such as the number of job placements made, then any changes in project funding might be compared to changes in employment statistics.

Regression analysis techniques or other mathematical methods may assist public sector auditors in comparing actual to expected results.

3.5.25 Audit Sampling (Chapter #7 of ISSAI #4000; paragraphs 172 to 178)

The auditor shall use audit sampling, where appropriate, to provide a sufficient number of items to draw conclusions about the population from which the sample is selected. When designing an audit sample, the auditor shall consider the purpose of the audit procedure and the characteristics of the population from which the sample will be drawn.

3.5.26 Evaluating Audits and Forming Conclusions (Chapter #8 of ISSAI #4000; paragraphs 179 to 190)

The auditor shall compare the obtained audit evidence with the stated audit criteria to form audit findings for the audit conclusion(s).

Based on the audit findings, and the materiality, the auditor shall draw a conclusion whether the subject matter is, in all material respects, in compliance with the applicable criteria.

The auditor shall communicate the level of assurance provided in a transparent way.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

Public sector auditors evaluate whether the evidence obtained is sufficient and appropriate so as to reduce audit risk to an acceptably low level. This evaluation includes exercising professional judgement and professional scepticism, and consideration of evidence that both supports, and seems to contradict, the subject matter information.

Evidence obtained is evaluated in relation to identified materiality levels in order to identify potential instances of material non-compliance. Determining the significance of findings is based on the concept of materiality as set out above. Findings from compliance audits must also be placed in proper perspective, for example reported instances of non-compliance may be based on the number of cases of noncompliance or the related monetary value (ISSAI #400, 4.0.19).

SAIs operating in a Court of Accounts environment have the ability to render judgement on the accounts. In cases of non-compliance, this may result in imposing reimbursements, fines or other penalties.

Public sector auditors evaluate whether, based on the evidence obtained, there is reasonable assurance that the subject matter information is in compliance, in all material respects, with the identified criteria. Due to the inherent limitations of an audit, public sector auditors cannot be expected to detect all occurrences of noncompliance.

Public sector auditors' assessment of what represents a material compliance deviation is a matter of professional judgement and includes considerations of context as well as quantitative and qualitative aspects of the transactions or issues concerned.

A number of factors are taken into account in applying professional judgement to determine whether or not the non-compliance is material. Such factors may include the:

- a) Importance of amounts involved (monetary amounts or other quantitative measures such as number of citizens or entities involved, carbon emissions levels, time delays in relation to deadlines, etc);
- b) Circumstances;
- c) Nature of the non-compliance;
- d) Cause leading to the non-compliance;
- e) Possible effects and consequences non-compliance may have ;
- f) Visibility and sensitivity of the program in question, (for example, is it the subject of significant public interest, does it impact vulnerable citizens, etc);
- g) Needs and expectations of the legislature, the public or other users of the audit report;

- h) Nature of the relevant authorities; and
- i) Extent or monetary value of the non-compliance.

Some examples of compliance deviations and considerations related to materiality and forming conclusions are set out in [Annex 9](#).

In evaluating evidence and forming conclusions, **written representations** may be obtained, as considered necessary in the circumstances, to support audit evidence obtained by public sector auditors. Such representations may state that the activities, financial transactions and information of the entity are in compliance with the authorities which govern them, or that particular control systems have functioned effectively throughout the period under audit.

Further guidance on written representations may be found in ISSAI #2580.

Public sector auditors perform audit procedures to determine if there are **subsequent events** that have occurred after the completion of the field work and up until the date of the compliance audit report that may result in material non-compliance, and therefore may require particular disclosure or may impact the auditor's conclusion or report.

Such procedures normally involve inquiry, obtaining written representations from management or reviewing relevant correspondence, minutes from meetings, published reports or financial information for subsequent periods (monthly, quarterly) etc. The amount of subsequent events work done may depend on the nature of the matters involved and the elapsed time between the completion of field work and the issuance of the report.

3.5.27 Requirements Related to Reporting (Chapter #9 of ISSAI #4000; paragraphs 191 to 209)

The auditor shall communicate the conclusion in an audit report. The conclusion can be expressed either as an opinion, conclusion, answer to specific audit questions or recommendations.

The auditor shall prepare an audit report based on the principles of completeness, objectivity, timeliness, accuracy and contradiction.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

Reporting is an essential part of a public sector audit and involves reporting deviations and violations so that corrective actions may be taken, and so that those accountable may be held responsible for their actions. To this end, the Fundamental Auditing Principles state that a written report, setting out findings in an appropriate form, should be prepared at the end of each audit (ISSAI #400, 4.0.7a).

The principles of completeness, objectivity and timeliness are important in reporting on compliance audits. Public sector auditors take care to ensure that reports presented are factually correct, and that findings are presented in the proper perspective and in a balanced manner. This involves applying the principle of contradiction which involves checking facts with the audited entity and incorporating responses from responsible officials as appropriate.

Form and Content of Compliance Audit Reports

The form of the written report may vary depending on the circumstances. However, some consistency in the auditor's report may help users of the report to understand the audit work done and conclusions reached, and to identify unusual circumstances when they arise.

The factors that may influence the form of the compliance audit report are numerous. These factors include, but are not limited to, the mandate of the SAI, applicable legislation or regulation, the objective of the particular compliance audit, customary reporting practice and the complexity of the reported issues. Furthermore, the form of the report may depend on the needs of the intended users, including whether the report is to be submitted to the legislature or to other third parties such as donor organisations, international or regional bodies, or financial institutions.

Depending on the above-mentioned factors, a SAI may find it appropriate to prepare either a short form report or a long form report. Long form reports (sometimes referred to as 'compliance audit special reports') generally describe in detail the audit findings and conclusions, including potential consequences and constructive recommendations, while short form reports are more condensed and generally in a more standardised format.

Guidance is given below on the form and content of reports. For the practical purposes of these standard, the illustrative examples provided in [Annex 10 to 14](#) are **short form reports**.

Due to the lengthy nature of long form reports, specific examples were not included in the standard.

In cases where the mandate of the SAI establishes a form of reporting that differs from that envisioned in these guidelines, the guidelines may, nonetheless, be useful to public sector auditors and may be applied, adapted as appropriate in the particular circumstances.

3.5.28 Report Structure – Direct Reporting Engagement (Chapter #9 of ISSAI #4000; paragraphs 201 to 217)

The audit report shall include the following elements (although not necessarily in this order):

- a) Title;
- b) Identification of the auditing standards;
- c) Executive summary (as appropriate);
- d) Description of the subject matter and the scope (extent and limits of the audit);
- e) Audit criteria;
- f) Explanation and reasoning for the methods used;
- g) Findings;
- h) Conclusion(s) based on answers to specific audit questions or opinion;
- i) Replies from the audited entity (as appropriate); and
- j) Recommendations (as appropriate).

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

Compliance Audit Reports

In general, the compliance audit report itself includes the following elements (although not necessarily in the following order):

1. **Title:** which clearly indicates the audit and its purpose;
2. **Addressee:** the person/organisation for whom the report is intended;

3. **Objectives and scope of the audit, including the time period covered:** what the audit covers;

4. **Identification or description of the subject matter information (and where appropriate, the subject matter):** details of the areas covered;

5. **Identified criteria:** The criteria against which the subject matter is assessed are identified in the auditor's report. In performing compliance audits, the criteria may differ greatly from audit to audit. Clear identification of the criteria in the compliance audit report is therefore important so that the users of the report can understand the basis for public sector auditors' work and conclusions. The criteria may be included in the report itself, or the report may make reference to the criteria if they are contained in an assertion from management, or otherwise available from a readily accessible and reliable source.

In cases where the criteria are not readily identifiable, or have had to be derived from relevant sources, the criteria applied in the audit are clearly stated in the relevant section of the auditor's report. In cases where the criteria are conflicting, the conflict is explained. In such a case, the potential consequences of the situation are explained to the extent possible and recommendations are provided as appropriate;

6. **Responsibilities of the various parties (legal basis):** who is responsible for what;

7. **Identification of the auditing standards applied in performing the work:** usually ISSAI;

8. **A summary of the work performed:** a brief overview of the work undertaken;

9. **A Conclusion:** depending on the scope and mandate of the audit, the conclusion may be expressed as a statement of assurance or as a more elaborated answer to specific audit questions. The nature of the wording may be influenced by the mandate of the SAI and the legal framework under which the audit is conducted.

Where no material instances of non-compliance have been identified, the conclusion is unqualified. An example of the form for an unqualified conclusion (where appropriate wording is inserted in the brackets as applicable) may be as follows:

'Based on the audit work performed, we found that [the audited entity's subject matter information] is in compliance, in all material respects, with [the applied criteria].'

Public sector auditors modify their conclusions appropriately in cases of:

a) Material instances of non-compliance. Depending on the extent of the noncompliance, this may result in:

i. A qualified conclusion (*'Based on the audit work performed, we found that, except for [describe exception], the audited entity's subject matter information is in compliance, in all material respects with [the applied criteria]...'*), or

ii. An adverse conclusion (*'Based on the audit work performed, we found that the subject matter information is not in compliance...'*); or

b) Scope limitation. Depending on the extent of the limitation, this may result in:

- i. A qualified conclusion (*'Based on the audit work performed, we found that, except for [describe exception], the audited entity's subject matter information is in compliance, in all material respects with [the applied criteria]...'*), or
- ii. A disclaimer (*'Based on the audit work performed, we are unable to, and therefore do not express a conclusion...'*)

Public sector auditors provide information as to the reasons for the modified conclusions. This may be done by describing the particular instances of significant non-compliance in the report, for example in a paragraph or section preceding the conclusion and that describes the basis for that conclusion.

Public sector auditors may conclude that there is a need to elaborate on particular matters which do not affect the compliance conclusion. In these circumstances, public sector auditors disclose these matters through the use of an:

- a) Emphasis of Matter paragraph (when the matter is presented and disclosed in the management assertions and is not materially misstated, for example to highlight a systematic weakness or an uncertainty dependent on future events such as when a competent authority has yet to determine if an item complies with the law); or
- b) Other Matter(s) paragraph (for matters other than those presented and disclosed in the management assertions, and not affecting the conclusion on compliance, for example the need for the legislature to take action when a conflict between different sources of law has been identified).

Examples are set out in [Annex 14](#).

10. Responses from the audited entity (as appropriate): incorporating responses from the audited entity by reporting the views of responsible officials is part of the principle referred to as the principle of contradiction. The principle of contradiction is a unique and important feature of public sector auditing.

It relates to the presentation of weaknesses or critical findings in such a way as to encourage correction (ISSAI #400, 4.0.20 and 4.0.24). This involves agreeing the facts with the audited entity to help ensure that they are complete, accurate and fairly presented. It may also involve, as appropriate, incorporating the audited entity's response to matters raised, whether verbatim or in summary.

11. Recommendations (as appropriate): the Fundamental Auditing Principles also emphasise the need for reports to be constructive. This means that the auditor's report may include, as appropriate, recommendations designed to result in improvements. While such recommendations may be constructive for the audited entity, they should not be of such a detailed nature that the public sector auditor's objectivity may be impaired in future audits (ISSAI #400, 4.0.4, 4.0.20 and 4.0.25).

12. Report date: The report is dated no earlier than the date public sector auditors have obtained sufficient appropriate audit evidence to support the conclusion.

13. Signature: The report is signed by the person with appropriate authority to represent the SAI. This may be the Auditor-General, an authorised officer, or possibly co-signatures of two officers to whom appropriate authority has been delegated.

Guidance on elements of a compliance audit report that warrant significant consideration by

public sector auditors are set out below.

Limited Assurance Reports

On an exceptional basis, these standards may be applied, adapted as appropriately, to limited assurance reviews. As explained in the scope section of these standards, in a limited assurance review, the conclusion (with appropriate wording inserted in the brackets as applicable) is normally expressed as follows:

‘Nothing has come to our attention that leads us to believe that [the audited entity’s subject matter information] is not in compliance, in all material respects, with [the applied criteria].’

Limited assurance reviews require a sufficient amount of work to be done in order to express a conclusion, albeit less work than that necessary to express a conclusion with reasonable assurance. Nonetheless, public sector auditors evaluate whether sufficient, appropriate audit evidence has been obtained in order to express a limited assurance conclusion.

Incidental Findings

Public sector auditors may often come across examples of non-compliance in connection with other types of audit work being performed. Even though the auditor was not actively looking for the existence or absence of the particular condition, public expectations might influence the decision to report such incidental findings.

Although public sector auditors may report such findings, these findings are outside the scope of the compliance audit. Unless the scope of the audit is re-evaluated and the incidental findings are incorporated into the ongoing compliance audit, the auditor does not obtain or provide reasonable assurance with respect to the existence or absence of the condition related to the incidental findings. It may, however, be possible to express a conclusion with limited assurance depending on the circumstances. In any event, when such situations are reported, it is important to inform the reader of the relevant assurance level (reasonable or limited), if any.

Compliance Audit Special Reports (Long Form Reports)

Depending on the needs of users, and the particular objective of the compliance audit, a SAI may decide to report the results of a compliance audit in a compliance audit special report. Such special reports are more akin to those reports common in performance audits and set out in greater detail the observations, conclusions and recommendations arising from the audit than the short form reports envisaged in the preceding section. In some cases, this type of report may be in addition to a compliance audit short form report.

As with compliance audit reports, some consistency in the form of compliance audit special reports may help users of the report to understand the audit work done and conclusions reached, and to identify unusual circumstances when they arise.

In general, compliance audit special reports include all of the elements set out in the guidance on compliance audit reports, but are normally structured into the following sections (the order of which may vary):

- a) **Title page:** The title page clearly sets out the title of the report, the report date, to whom the report is addressed and the preparer of the report. The preparer of the report is normally the SAI. Including a table of contents, especially if the report is voluminous, helps give the report structure and guide the reader to areas of particular interest. A glossary may also be helpful to readers if technical or unfamiliar terminology, acronyms, abbreviations or words with a particular

contextual meaning are used repeatedly throughout the report.

b) **Table of Contents:** ideally with hyperlinks to sections;

c) **Glossary:** if necessary;

d) **Executive Summary:** The executive summary is critical as it is often the part of the report most read by users. The executive summary should reflect fully and accurately, while at the same time in a concise and balanced fashion, the content of the report. To be effective, an executive summary is normally one to two pages in length. The main focus of the executive summary is on the identified criteria (significant questions to be answered) and a summary of the main audit conclusions and recommendations in relation to such criteria (answers to the questions).

In some cases, a chart or diagram may display significant audit conclusions in a form that makes it easier for users to grasp complicated or voluminous information. In such cases it may be helpful to users to include graphical information in the executive summary.

e) **Introduction, Objectives and Scope:** The introduction sets out the context of the audit including the objectives and scope of the audit, identification or description of the subject matter or subject matter information, the identified criteria, the responsibilities of the various parties involved and the auditing standards applied in performing the work.

The introduction is generally short without a lot of detail. If necessary, relevant detailed information may be included in appendices.

f) **Observations and Findings:** The observations and findings section comprises the main body of the compliance audit special report. This section describes the audit work performed and related findings. It is structured in a logical manner, normally around the identified criteria, and in a way that assists the reader in following the logical flow of a particular argument.

When presenting audit observations and findings, making the following four elements apparent to users assists them in gaining a better understanding of the audit work performed and the significance and consequences of the audit findings:

- i) **Criteria:** the benchmark or measure against which performance is compared or evaluated
- ii) **Conditions:** the situation observed;
- iii) **Cause:** the source and reasons giving rise to the conditions observed;
- iv) **Effect:** the impact and consequences of the conditions observed (the materiality of the findings, their impact on the budget, citizens or users, implications for principles of sound public sector management, etc).

When significant amounts of data are included to support audit findings, such data may be more appropriately included in appendices.

g) **Conclusions and Recommendations:** The primary purpose of the conclusions and recommendations section of the report is two-fold:

- i) to provide clear answers (conclusions) to the audit questions (identified criteria), and

ii) to provide constructive and practical recommendations for improvement where appropriate.

Recommendations are most effective when they are positive in tone and results-oriented, setting out clearly what needs to be done, when and by whom. Cost considerations are borne in mind when determining the practicality of recommendations.

Where significant compliance deviations are reported, recommendations are provided in cases where there is potential for significant improvement. It may be helpful to users for public sector auditors to highlight ongoing corrective actions.

While constructive and practical recommendations assist in promoting sound public sector management, public sector auditors are careful not to provide such detailed recommendations so as to be taking on the role of management and thereby impairing their own objectivity.

h) Responses from the Audited Entity: The **principle of contradiction** – agreeing facts and incorporating responses – should be applied in preparing compliance audit special reports. Responses from the audited entity to matters raised may be incorporated in the report, either verbatim or in summary.

Responses from the audited entity may be included in a separate section of the special report or as an appendix, depending on the volume of the responses.

Incorporating the views of responsible officials assists in ensuring the practicality of the recommendations and in making the responsible officials accountable for their actions.

i) Appendices: Where appropriate, appendices may be used to provide users with detailed or supplementary information related to the audit. The information may be in text or table format, or it may be more graphical in nature such as diagrams, charts or pictures. Such information may assist users in understanding the audit findings, as well as the causes and effects thereof.

3.5.29 Report Structure – Attestation Reporting Engagement (Chapter #9 of ISSAI #4000; paragraphs 218 to 220)

The audit report shall include the following elements (although not necessarily in this order):

- a) Title;
- b) Addressee;
- c) Description of the subject matter information, and when appropriate the underlying subject matter;
- d) Extent and limits of the audit including the time period covered;
- e) Responsibilities of the responsible party and the auditor;
- f) Audit criteria;
- g) Identification of the auditing standards and level of assurance;
- h) A summary of the work performed and methods used;

- i) Opinion/conclusion;
- j) Replies from the audited entity (as appropriate);
- k) Report date; and
- l) Signature.

3.5.30 Additional Reporting Structure – SAI with Jurisdictional Powers (Chapter #9 of ISSAI #4000; paragraphs 221 to 224)

In the SAIs with jurisdictional powers, the auditor shall consider the role of the prosecutor or those responsible for dealing with judgment issues within the SAI, and shall also include as appropriate, the following elements in both direct reporting and attestation engagements:

- a) Identification of the responsible parties and the audited entity;
- b) The responsible person(s) involved and their responsibilities;
- c) Identification of the auditing standards applied in performing the work;
- d) Responsibilities of the auditor;
- e) A summary of the work performed;
- f) Operations and procedures etc. that are affected by non-compliance acts and/or possible unlawful acts. This needs to include, as appropriate:
 - A description of the finding and of its cause,
 - The legal act which has been infringed (the audit criteria),
 - The consequences of the non-compliance acts and/or possible unlawful acts.
- g) The responsible persons and their explanations regarding their noncompliance acts and /or possible unlawful acts, when appropriate;
- h) The auditor's professional judgment which determines whether there is personal liability for non-compliance acts;
- i) The value of the loss/misuse/waste created and the amount to be paid due to personal liability
- j) Any measures taken by responsible persons during the audit to repair the loss/misuse/waste created; and
- k) The management's arguments on the non-compliance/unlawful acts.

3.5.31 Considerations Related to the Reporting of Suspected Unlawful Acts (Chapter #9 of ISSAI #4000; paragraphs 225 to 231)

In conducting compliance audits, if the auditor comes across instances of non-compliance which may be indicative of unlawful acts or fraud, s/he shall exercise due professional care and caution and communicate those instances to the responsible body. The auditor shall exercise due care not to interfere with potential future legal proceedings or investigations.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

While detecting potential unlawful acts, including fraud, is normally not the main objective of performing a compliance audit, public sector auditors do include fraud risk factors in their risk assessments, and remain alert for indications of unlawful acts, including fraud, in carrying out their work.

In performing compliance audits, if public sector auditors come across instances of non-compliance which may be indicative of unlawful acts or fraud, they exercise due professional care and caution so as not to interfere with potential future legal proceedings or investigations. Public sector auditors may consider consulting with legal counsel or appropriate regulatory authorities (ISSAI #300, 3.4.7).

Furthermore, they may communicate their suspicions to the appropriate levels of management or to those charged with governance, and then follow up to ascertain that appropriate action has been taken. In regard to instances of non-compliance related to fraud or serious irregularities, because of the different mandates and organisational structures that exist internationally, it is up to the SAI to determine the appropriate action to be taken (ISSAI #400, 4.0.7b).

Due to the inherent limitations of an audit, there is an unavoidable risk that unlawful acts, including fraud, corruption or theft may occur and not be detected by public sector auditors. Fraud may consist of acts designed to intentionally conceal its existence.

There may be collusion between management, employees or third parties, or falsification of documents. For example, it is not reasonable to expect public sector auditors to identify forged documentation in support of claims for grants and benefits, unless they are reasonably obvious forgeries.

In addition, public sector auditors may not have investigative powers or rights of access to individuals or organisations making such claims.

Only a court of law can determine whether a particular transaction is illegal. Although public sector auditors do not determine if an illegal act has occurred, they do have a responsibility to assess whether the transactions concerned are in compliance with applicable laws and regulations.

Fraudulent transactions are, by their nature, not in compliance with the applicable law. Public sector auditors may also determine that transactions where fraud is suspected, but not yet proven, are not in compliance with the applicable law.

Material unlawful acts normally result in a modified audit opinion or conclusion.

If suspicion of unlawful acts arises during the audit, public sector auditors, where permitted by law, may communicate to the appropriate levels of management and those charged with governance. In this case, those charged with governance are likely to be ministerial or administrative bodies higher up in the reporting hierarchy.

Public sector auditors follow up and ascertain that management or those charged with governance have taken appropriate action in response to the suspicion, for example by reporting the incident to the relevant law enforcement authorities. Public sector auditors may also report such incidents directly to the relevant law enforcement authorities.

3.5.32 Requirements Related to Follow-Up (Chapter #10 of ISSAI #4000; paragraphs 232 to 236)

The auditor shall decide follow-up on opinions/conclusions/recommendations of instances of non-compliance in the audit report when appropriate.

The following paragraphs are not part of the current standard but have been extracted from the previous standard #4100 as they provide valuable additional information.

The Fundamental Auditing Principles place emphasis on the reporting of constructive recommendations and additional follow-up as necessary in regard to correction of identified weaknesses (ISSAI #400, 4.0.26). The need for any follow-up of previously reported instances of non-compliance will vary with the nature of the non-compliance and the particular circumstances. This may include formal reporting by the auditor to the legislature, as well as to the audited entity or other appropriate bodies. Other follow-up processes may include reports, internal reviews and evaluations prepared by the audited entity or others, a follow-up audit, conferences and seminars held for, or by, the audited entity, etc. In general, a follow-up process facilitates the effective implementation of corrective actions and provides useful feedback to the audited entity and to the users of the report and to public sector auditors in planning future audits. Follow-up processes may be set out in the mandate of the SAI.

3.6 GUID #4900 - #4999: Supplementary Compliance Audit Guidelines

GUID #4900 is currently at the Exposure Draft stage. The objective of this GUID will be to provide support to the auditor in planning, executing and reporting on adherence to regularity and propriety criteria in a compliance audit.

PART THREE: TYPES OF COMPLIANCE AUDITING

Chapter 4: Compliance Auditing Related to the Audit of Annual Financial Statements

This chapter covers: [Overview](#); [Controllership](#), [Planning](#); and [Systems Audit](#).

4.1 Overview

4.1.1 Background

For most SAI, the large majority of the compliance audit work that they undertake will fall into this category. The main reason for the existence of a SAI is to audit the Annual Financial Statements (AFS) and to form an opinion and report on those AFS.

The work on the actual AFS can only begin once the Ministry of Finance has produced them and, typically, the SAI has three months to form its opinion and report. What is it going to do for the remaining nine months? This answer is, of course, interim audit work on the AFS.

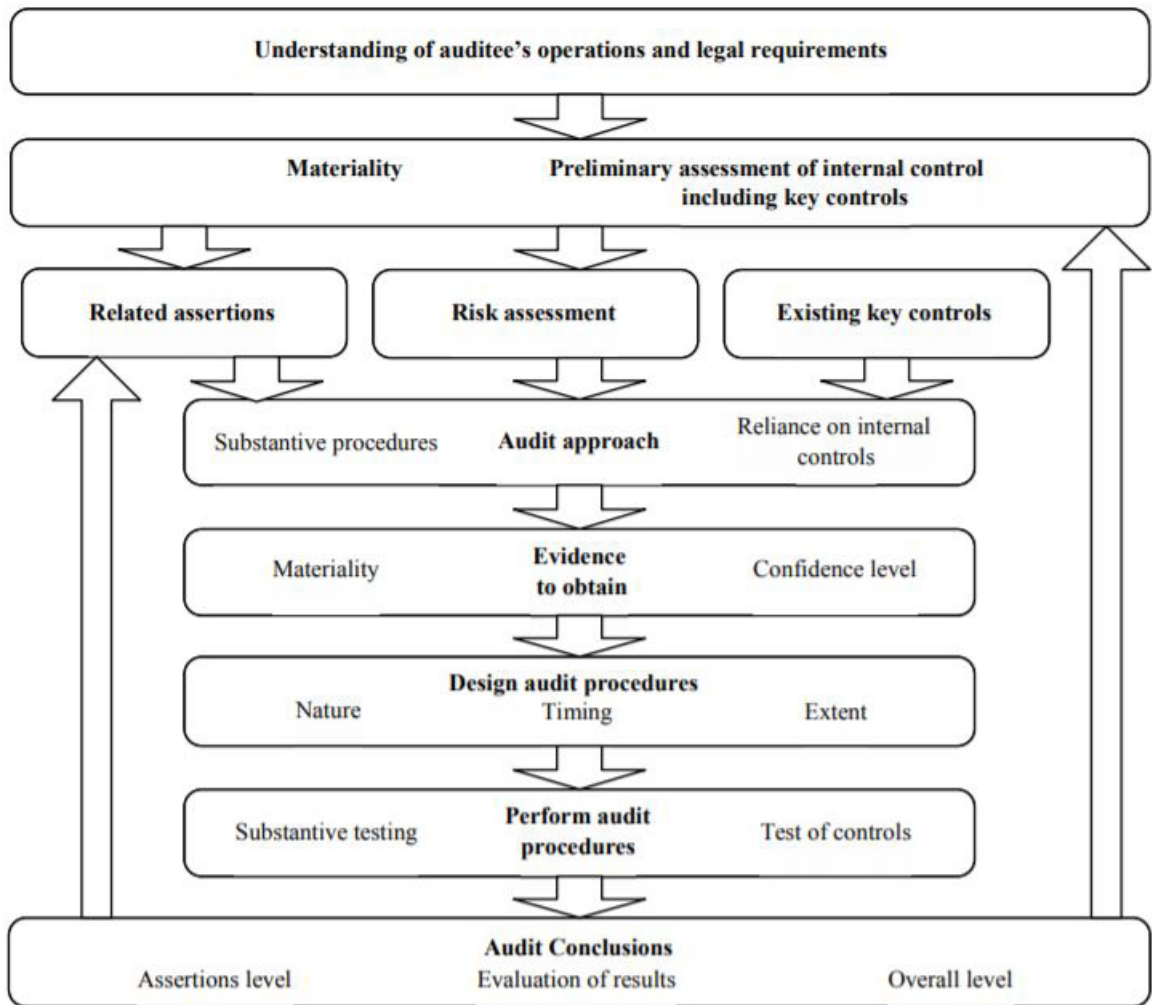
Simplistically, this involves ensuring that the financial data emerging from major systems and finding its way into the AFS can be relied upon. This, in turn, requires the auditor to assure themselves that the system is both sound (“fit for purpose”) and that it is followed (**complied with**).

Thus, the interim audit process involving auditing the systems of the organisation being audited is **Compliance Auditing Related to the Audit of AFS**.

This involves:

- **Identifying the Systems:** all systems for each component of the audited entity have to be identified and classified;
- **Planning the Audit of the Systems:** as part of the overall planning process for the financial audit, provision has to be made for the compliance audit of the systems;
- **Undertaking the Audits:** the audits must be undertaken in accordance with ISSAI; and
- **Using the Results:** the SAI must use the results as part of its opinion forming process.

Figure 18: Detailed Audit Process



Source: ECA Financial and Compliance Manual

4.1.2 Controllership

Although only relevant to New Zealand¹² and Samoa, the Controllership role of the SAI, when it exists, provides a further element of Compliance Audit in support of the AFS audit.

This description of the Controllership function, which provides assurance that spending by government departments is in keeping with Parliament's expectations and funding amounts, has been extracted from the New Zealand Controller and Auditor-General's website.

“Although New Zealand has an elected Government in power, the Government alone doesn't decide what New Zealanders' taxes will be spent on. The whole of Parliament is involved (all of the elected representatives) in decisions about how much money will go to different areas of spending (such as spending on health, or education, or conservation, or defence).

The approved decisions about what the Government can spend money on are recorded in what are known as “appropriations”. Those appropriations become law, so spending that doesn't fit within an appropriation (because too much was spent or money was spent on activities that the appropriation didn't cover) is unlawful.

The checks that take place

During annual audits of government departments, auditors check that spending is in keeping with the amounts and the types of activity set out in the appropriations. If it doesn't look right, auditors raise that with us (the Office of the Auditor-General) and with those in charge of the department that has made mistakes in its spending.

The fix that needs to be applied depends on whether the spending was too high or on the wrong sort of activity. Fixing these sorts of errors can be complicated but the fix must be done correctly because these are matters of law.

As well as these checks during the audits, the Treasury sends us monthly reports to review. We get highly detailed spreadsheets of the spending done by government departments, and we check them.

The Controller's powers

If the Controller is not satisfied with the steps that a government department is taking to fix an appropriation error, he can stop the government department from receiving money.

The Controller can also direct a Minister to report to Parliament about the wrongful spending.

This power is a very important part of New Zealand's system of democracy. It means that someone is watching the spending that happens and can "turn off the money tap" if that spending isn't lawful."

Thus, it can readily be seen that this function, where it exists, is an important adjunct to the other areas of Compliance Auditing is support of the AFS audit discussed below.

4.2 Planning

4.2.1 Introduction

Audit manuals often have very complex methodologies for developing audit plans. However, this manual as this aimed at the smaller PASAI members it is deliberately using a much simpler model for two main reasons:

- **Resources:** the smaller SAI do not have the resources to spend in undertaking complex planning process; and
- **Skills:** they may also lack the necessary skills.

If a SAI does want to follow more complex models such as that described in the INTOSAI Development Initiative (IDI)'s Compliance Audit Implementation Handbook, some of which material is incorporated here, it is, of course, free so to do.

The approach suggested here identifies the systems which need to be audited to determine the level of compliance and how this will affect the opinion on the Annual Financial Statements (AFS) and uses a combination of risk-based and judgement-based approaches to prioritise them.

4.2.2 Strategic Audit Plan¹³

There should be a **rolling Five Year Strategic Plan** from which an Annual Plan will be derived. The Annual Plan can be divided into quarterly plans, if required.

A Strategic Plan is necessary because it is impossible to audit every aspect of every organisation each year. It is important to have a plan which will ensure that nothing obvious is overlooked over the long-term cycle of the audit.

¹³ This is just a brief summary of this important SAI management process and more detailed guidance is provided elsewhere such as the IDI Strategic Management Handbook <https://www.idi.no/en/idi-library>

Such plans will need to be flexible because, as the audit progresses, fresh or better information will come to light which will result in a review of the priorities given to each area of work. This review needs to be a continuous exercise throughout the audit and the Strategic Plan updated accordingly.

Comprehensive review of all possible audit requirements can be assured by preparing a list of all separate jobs appropriate to the particular organisation.

The Strategic Plan will, thus, contain **items which must be audited every year and items which will be looked at only once or twice over the five-year audit cycle and items which will only be looked at on a one off basis/when a risk or issue arises.**

The Strategic Plan should be of a rolling nature and be updated annually to run for a further five years rather than being a series of discrete five-year plans.

4.2.3 Formulating the Strategic Plan

The initial two areas which have to be developed for effective Strategic Planning:

- **Clients and Systems:** a comprehensive database needs to be developed of all clients and all major systems used by these clients requiring separate audit. This can either be from personal knowledge; the audit files or undertaking a formal “Overall Review”; and
- **Work Required:** based on a risk analysis of the systems, work other than final accounts be classified as Fundamental (to be undertaken every year); Non-fundamental (every two or three years) or Minor (every four or five years).

Certain work will be required **every year:**

- **Planning:** time should be allocated to updating the Strategic Plan and extracting and developing the Annual Plan;
- **Administration:** time should be allocated to keeping the plan updated; circulating the draft reports; meetings on the reports, etc.;
- **Reserve:** some time should always be kept in reserve to cover over-runs in audits to for new work which becomes necessary after the plan has been drawn up (10% is a reasonable figure to use); and
- **Final Accounts:** the SAI is required to audit the annual financial statements and certify them.

Other work will be “**cyclical**” and will only be audited in accordance with the Strategic Plan. Each system of each client should be risk assessed and a decision made as to whether it is a **Fundamental (Major); Non-fundamental or Minor System** and how many times it should be audited in the cycle.

The development of a Strategic Audit Plan, dividing this area of work into three sections (**Fundamental systems, Non-fundamental systems, and Minor systems**), each of which would have a different incidence of auditing, will be a move in the desired direction. The goal here is to ensure that audit reports are issued for each compliance audit undertaken and that these contain sufficient details of the findings and recommendations to primary accounting systems, internal controls and disclosures in their financial statements to support the opinions given therein.

4.2.4 Audit Resources Required

Having identified all the clients and all the systems, the next part of the Strategic Planning Process is to estimate how many man-days will be required to undertake the work if every system were to be audited completely over the cycle – the ideal situation.

This should be based on past knowledge adjusted for new staff skills and will require a high degree of estimation initially. However, after two or three years, it should be possible to refine the number of days required to produce a more accurate model. It is most unlikely that there will be enough man-days available to complete every audit to the depth required which is where the analysis in the next section comes in.

However, the shortfall in staff resources is a vital piece of information. Parliament has laid down the mandate it requires the SAI to fulfil. Thus, in theory, it should provide the resources necessary for it to do so. The shortfall can be used to support requests for further staff resources.

The Strategic Plan should now look like Figures 19 and 20. Figure 19 is for a single client (the Ministry of Administrative Affairs) and Figure 20 is the Summary Strategic Plan for the National Audit Office as a whole. The use of an Excel spreadsheet for this is strongly recommended. Thus, the Summary Strategic Plan will come automatically from, and be the sum of, the individual client Strategic Plans.

Figure 19: MINISTRY STRATEGIC AUDIT PLAN

Client: Ministry of Administrative Affairs

Prepared/Amended by	Date	Comment

P – Planned; A – Actual

Area of Work	Total Time	2021		2022		2023		2024		2025		Comments
		P	A	P	A	P	A	P	A	P	A	
Planning		20		20		20		20		20		
Administration		15		15		15		15		15		
Reserve		40		40		40		40		40		
Final Accounts		100		100		100		100		100		
Cyclical												
- Fundamental		110		110		110		110		110		
[NB List all Fundamental Systems below; work to total 110 days]												Each system audited every year.
- Non-fundamental		70		70		70		70		70		
[NB List all Non-Fundamental Systems below; work to total 70 days]												Each system audited twice over 5 years
- Minor		30		30		30		30		30		
[NB List all Minor Systems below; work to total 30 days]												Each system audited once over 5 years
TOTAL (to Annual Control)		385		385		385		385		385		

Figure 20: SUMMARY STRATEGIC AUDIT PLAN

Prepared/Amended by	Date	Comment

P – Planned; A – Actual

Area of Work	Total Time	2021		2022		2023		2024		2025		Comments
		P	A	P	A	P	A	P	A	P	A	
Planning		350		350		350		350		350		
Administration		175		175		175		175		175		
Reserve		465		465		465		465		465		
Final Accounts		1500		1500		1500		1500		1500		
Cyclical												
- Fundamental		1300		1300		1300		1300		1300		
- Non-fundamental		800		800		800		800		800		
- Minor		250		250		250		250		250		
TOTAL (to Annual Control)		4840		4840		4840		4840		4840		

NB Actual figures for 2021 will be entered as jobs are completed; the plan is a rolling plan with completed years being retained for reference.

4.2.5 Annual Audit Plan

The Annual Audit Plan will determine which systems are subject to compliance audit in the current year. **Major systems** will require auditing every year. Thus, the SAI would be expected, for example, to audit the payroll of one or more large ministries each year (see [Annex 1](#)). It would also be expected to audit major revenue and funding sources (see [Annex 2](#)) and capital expenditure, etc. see [Annex 3](#)).

Non-fundamental and Minor systems will only be audited in specific years and some minor systems where amounts are immaterial may never be audited as the costs would outweigh any possible losses.

When deciding which systems to audit, the SAI will use a form of risk analysis. Initially, the risk analysis can be fairly basic based on the amounts involved in the systems; past history of problems with the systems; audit “nose”; etc. but, over time, more sophisticated, mathematical-based systems should be developed.

In performing these later policy and risk review, the auditor may consider, among others, the following:

- **Stakeholders Priorities and Interests:**

- Public or legislative interests or expectations, e.g. achievement of Sustainable Development Goals (SDG) by the country;
- Interest of and impact on citizens;
- Interests of beneficiaries of public funds;
- Media coverage; and
- Non-compliance signalled by third parties.
- **Changes to the legal framework and other developments in the area, for example:**
 - Developments/changes in the legal framework in the different areas;
 - Significance of certain provisions of the law;
 - Principles of good governance;
 - Other major/important changes and developments in the different areas;
 - Roles of different public sector bodies and changes thereto;
 - Rights of citizens and of public sector bodies;
 - Potential breaches of applicable laws and other regulations that govern the public entity's activity, or the public debt, public deficit and external obligation and
 - Projects with significant public funding.
- Results of recent audits and developments in audit, including:
 - Non-compliance with internal controls, or the absence of an adequate internal control system;
 - Findings identified in previous audits of the SAI;
 - Works of other SAI;
 - Developments in audit; and
 - Mandate and audit coverage of the SAI.

Compliance audit is risk based and you need to bear in mind that risk-based approach should be applied to identify the subject matters. It is essential that the SAI rather spend the scarce resources on the audits where the risk is high and that the subject matter is significant/material to the intended user(s). Therefore, it is recommended that, where the SAI has discretion to select the subject matter, compliance audits based on ISSAI #4000, should be carried out only where there is high risk or that the subject matter is significant, and these should be prioritised at the SAI level. It is not necessary to carry out compliance audit for the same subject matter annually for each entity unless it is a requirement in the SAIs mandate. When the subject matter is prioritised/ranked at the SAI level, it is also possible to avoid audits that have low impact and that are immaterial to the intended users.

Figures 21-23 provide guidance as to how this process could take place.

Figure 21: Identification of Potential Audit Tasks and Their Ranking

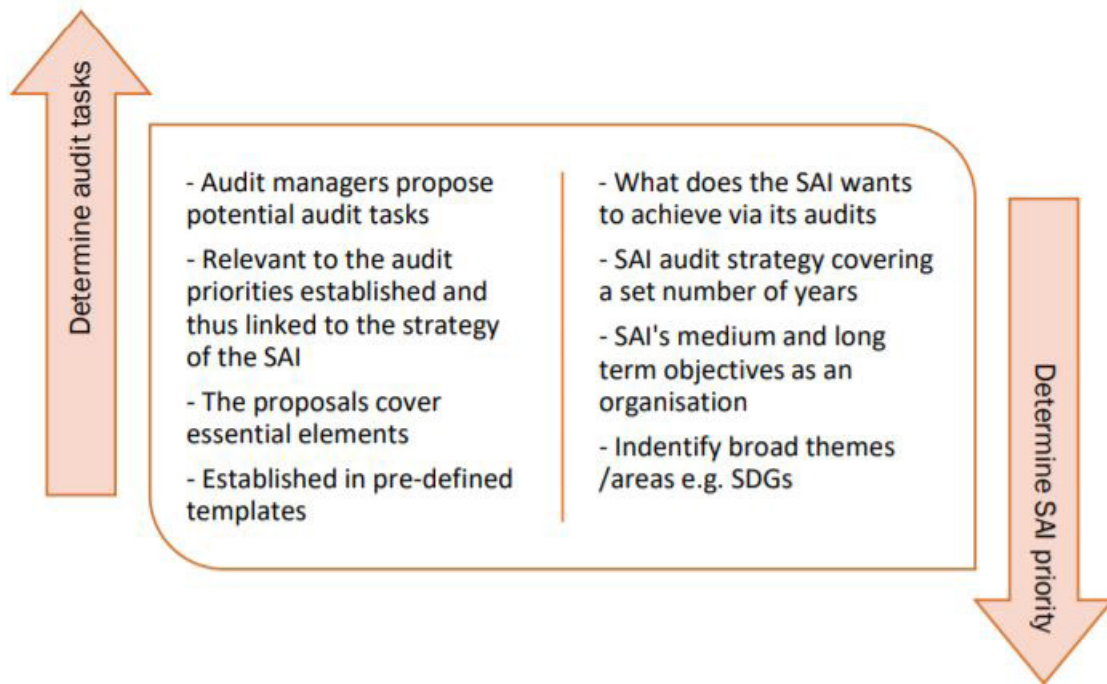


Figure 22: Determining the Importance of Risk

		Likelihood of occurrence	
		Low	High
Potential Impact	Substantial	Medium Risk	High risk
	Minimum	Low risk	Medium risk

Figure 23: Priority Ranking of a Task

Audit task:								
Priority		Risk		Interest		Added value		
N/R	Score 0							
Low	Score 1	Low	Score 0	Low	Score 0	Low	Score 0	
Medium	Score 2	Medium	Score 1	Medium	Score 1	Medium	Score 1	
High	Score 3	High	Score 2	High	Score 2	High	Score 2	
Total Score:								

4.2.5 Individual Audit Plan

This section provides an example of Compliance Audit Planning for a specific audit – procurement. The separate case study provides more detail on identifying criteria for benchmarking and developing the audit questions to ask to complete the compliance audit.

The audit plan's components – areas, activities, systems, structures to be audited – should be selected based on the compliance criteria whose fulfilment by the audited entity is to be confirmed.

For audits of compliance with procurement legislation, it should be determined whether these will be end-to-end audits of the procurement process, from planning to delivery, or whether only a part of the process (e.g. fulfilment of contractual obligations) is to be audited.

Each of the sub-activities in the procurement cycle has its own objectives that are directly linked to legal requirements. Therefore, the components of the audit plan should correspond to each major legal requirement for **procurement** (see Table 8).

Table 8: Compliance Audit Planning

Audit Plan Component	Audited Entity's Compliance Obligation	Audit Objective
Procurement Planning: <ul style="list-style-type: none"> • Link to the Strategic and Medium Term Plan; • Needs assessment; • Procurement strategy; • Resource planning; • Development of technical specifications. 	List of relevant legal regulations for each component: <ul style="list-style-type: none"> • Public Procurement Law; • Budget Code; • Annual Budget Law; • Internal procedures, etc. 	Lawfulness and regularity
Audit plan component	Audited entity's compliance obligation	Audit objective
Tender Committee's Work: <ul style="list-style-type: none"> • Tender committee regulations; • Qualification of members; • Capability and capacity to adhere to legal requirements. 	See above	Lawfulness and regularity
Economy, efficiency and effectiveness provided by the tender procedure: <ul style="list-style-type: none"> • Selection of appropriate tender procedures; • Technical specifications, terms of reference and contractual conditions that guarantee and protect the public entity's interests. 	See above	Lawfulness and regularity
Execution of Procurement Contracts: <ul style="list-style-type: none"> • Control and monitoring of compliance with contractual conditions and technical specifications; • Proper recoding of acquisitions, payables and receivables on the balance sheet and the expenditures account. 	See above	<ul style="list-style-type: none"> • Lawfulness and regularity; • Completeness; • Ownership; • Measurement.

Planning for individual compliance audits includes preparing the audit strategy and an audit plan. Preparation of audit strategy for the identified audit entity would include:

- An understanding of the auditable entity and its internal control environment, including the statutory, regulatory and legal framework applicable to the auditable entity and the applicable rules, regulations, policies, codes, significant contracts or agreements etc;
- An understanding of relevant principles of sound public sector financial management and expectations regarding the conduct of public sector officials for propriety related issues;
- Identification of the intended users, including responsible party and those charged with governance;
- Consideration of materiality and risk assessment including suspected unlawful acts or fraud;
- Determining the scope of audit with reference to the selected specific subject matter, if selected, as well as proprietary concerns;
- Development of audit objectives for the specific subject matter, if selected;
- Identification of audit criteria for specific subject matter;
- Sampling considerations, specifically for implementing units below the selected audit units; and
- Considerations related to direction, supervision and review of the audit team(s).

Once the audit strategy is in place, the audit plan could be prepared. The plan for the identified auditable entity would include:

- Description of selected audit units;
- Sample selection of implementing units under the selected audit units;
- Extent of audit in each selected unit;
- Timing of audit;
- Formation of audit team/s (in case more than one audit team is needed for the auditable entity);
- Assignment plan detailing the duties of the audit team members;
- Planned audit procedures; and
- Potential audit evidence to be collected during the audit.

Both the overall audit strategy and the audit plan should be documented in the audit file. Planning for individual compliance audits is a continual and iterative process. The overall audit strategy and plan are therefore required to be updated as necessary throughout the audit.

4.3 Systems Audit

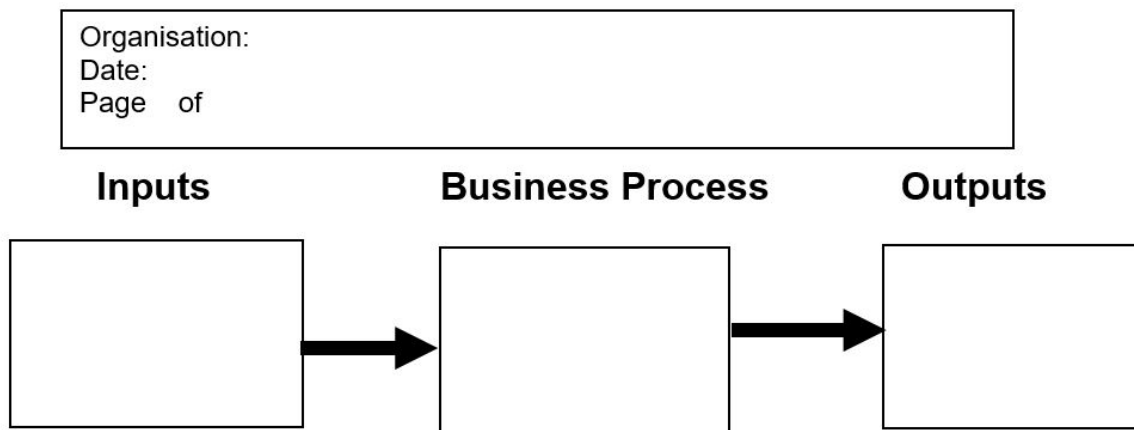
4.3.1 Definition

A system may be defined as:

“a series of related procedures designed to achieve some overall objective”.

All systems are composed of the same basic elements: **inputs, processes and outputs**. The auditor is concerned to ensure that adequate authorisation and control exist at each stage of the operation. The auditor wants to ensure that each system is as accurate and efficient as possible.

Figure 24: Management Overview Diagram



There are two types of procedures within a system:

- **Accessing Procedures:** which aim to move a transaction through a system; and
- **Control Procedures:** which aim to:
 - ensure processing operates in an orderly manner;
 - statutory and management requirements are complied with;
 - the organisation's assets are safeguarded; and
 - the completeness and accuracy of records is secured.

Systems Audits is concerned with **control procedures**. A basic test is for the auditor to ask whether the procedure contributes to the final output. If the answer is "no", it is probably a control procedure.

4.3.2 Responsibility for Systems

It is management, **not** the auditor, who is responsible for ensuring that there are sound, efficient systems within an organisation.

If the auditor designs a system it is difficult for him to adopt an independent approach to its subsequent review.

Also, staff operating it may resent an "audit imposed" system and deliberately fail to operate it correctly.

Nonetheless, there may be times, especially with regard to organisations with poor management, when the auditor has to design the system as he knows it is beyond the management's ability. There is little point in criticising a system when you know management is incapable of improving it.

4.3.3 Stages of Systems Audit

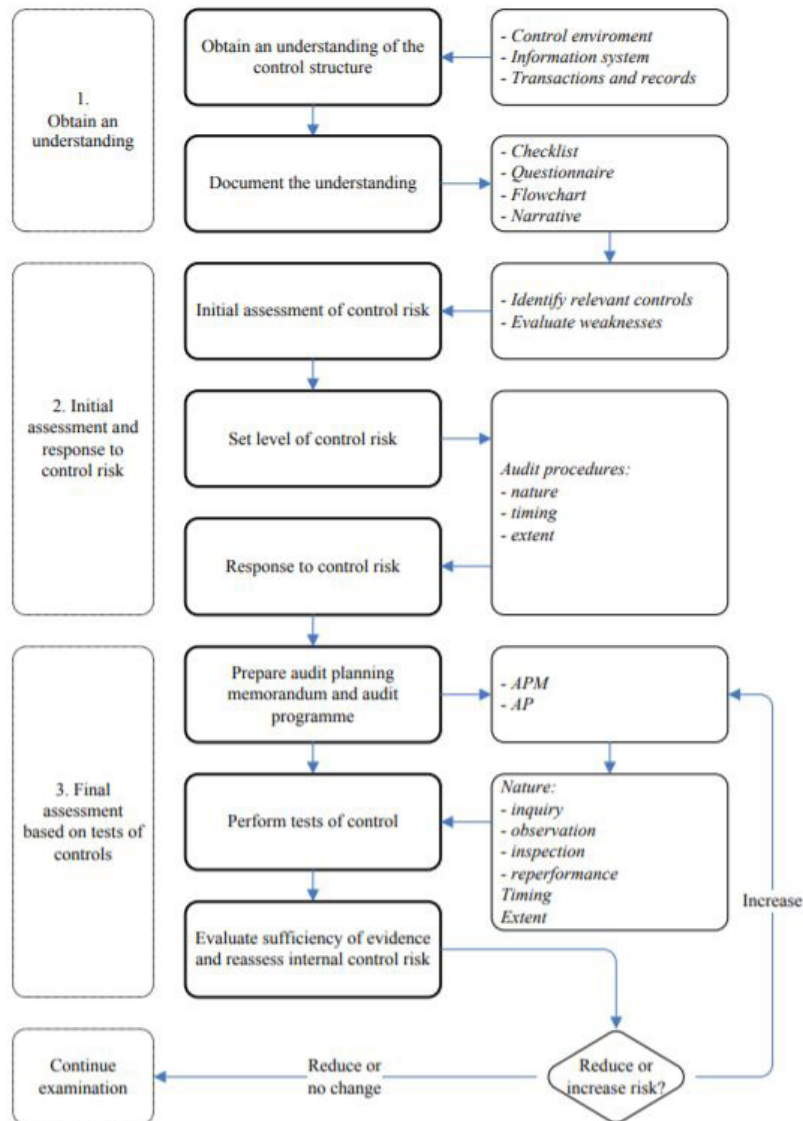
There are six main stages to a systems audit:

- Identifying the main Financial Systems;
- Recording the Systems;
- Testing the Systems;

- Reviewing Controls and identifying Weaknesses;
- Improving the System; and
- Compliance Testing and Reviewing.

One golden rule in systems auditing is that the control should never cost more to operate than the likely loss if it did not exist.

Figure 25: Tests of Controls



Source: ECA Financial and Compliance Audit Manual

4.3.4 Identifying Major Financial Systems

These will obviously vary with the organisation concerned. However, a major financial system will deal with a significant part of the income, expenditure or asset holding of the organisation.

Examples include: payroll, creditors, debtors, cash and bank, stores, inventories, investments, budgetary preparation and control, project appraisal, capital expenditure and manpower controls.

4.3.5 Recording the System

These can either be in written form or flowcharts or a combination of the two. Probably the best way is by using flowcharts.

4.3.6 Testing the System

This is to test whether the system actually works as laid down in the systems specification or flowchart.

It is tested by selecting a sample of transactions and “walking them through” the system. Any deviation from the system as laid down can be recorded and an accurate picture built up of how the system actually works.

4.3.7 Reviewing Controls and Identifying Weaknesses

When reviewing controls it is necessary to concentrate on “key” controls. These are controls which are essential for the achievement of the control objective and the absence of which could give rise to material loss or error.

Having determined which parts of the system should have key controls it is necessary to establish their existence. The absence of an expected control on a major part of a system is a significant weakness.

Where a key control does exist, whether it is doing its job properly needs testing via the existence of “after-the-fact” evidence such as a regular report output.

If expected controls are absent are there other, compensating, controls elsewhere in the system giving the same level of protection?

Controls which are unnecessary or inefficient should be highlighted for management action.

4.3.8 Improving the System

Where control weaknesses and inefficient or unnecessary procedures have been identified they should be drawn to management’s attention and recommended improvements suggested.

If management refuses to act to improve the system, record the weakness in a memorandum, pointing out the manager’s rejection of them and stating that he takes full responsibility for anything that goes wrong with the system in future. This not only covers the auditor but also usually makes the manager reconsider his position!

4.3.9 Compliance Testing and Reviewing

It is necessary, at regular intervals, to **test compliance with the agreed system**, particularly with the key control features.

Internal Control Questionnaires are a useful means of undertaking compliance testing.

It is also necessary to review the system periodically, in the light of changing circumstances, to make sure that controls continue to be relevant and up to date.

4.3.10 Examples of Review Areas

When reviewing major systems, the auditor will be testing for items such as those listed below. This is not an exhaustive list and SAI will know the potential weaknesses in their own

jurisdiction's and test accordingly. These include:

- **Expenditure:** to ensure that this is in line with the budget as passed by parliament; for payroll look for ghost employees, false overtime claims;
- **Revenue Collection:** ensure that all revenue due is collected and accounted for and that, where based on charges, these reflect cost (if appropriate) and that they are regularly reviewed;
- **Procurement:** that procurement policies are duly followed and not circumvented by, for example, splitting orders (see Case Study); and
- **Assets:** their existence, valuation and that they are not misused (e.g. private use of government vehicles).

Audit checklists covering some of the above issues are annexed to this Manual as follows:

- [Annex 19](#): Payroll Audit;
- [Annex 20](#): Payment of Creditors;
- [Annex 21](#): Cash Control;
- [Annex 22](#): Land and Buildings Register;
- [Annex 23](#): Stocks, Stores and Supplies; and
- [Annex 24](#): Capital Schemes Investigation.

Chapter 5: Stand Alone Compliance Auditing

The key points are: [Introduction](#); [One-off Compliance Audits](#); [Performance Audits](#); [Budget Audits](#); [Donor Funded Projects](#); and [Social Responsibility Audits](#).

5.1 Introduction

As indicated the previous chapter, the vast majority if compliance audit work will be undertaken in conjunction with the financial audit to form an opinion on the Annual Financial Statements (AFS). However, there are occasion where compliance audits not associated with AFS can be undertaken.

The main types of such audits are:

- **One-off Compliance Audits:** possibly arising from requests from Government or Parliament;
- **Performance Audits:** will usually include compliance audit elements;
- **Budget Audits:** reporting on the budget prior to its passing by Parliament;
- **Donor Funded Projects:** where some or all of the expenditure is externally funded by loan or grant; and
- **Social Responsibility Audits:** a new and growing area of audit activity.

Specific Legislative Requirement: a standard audit compliance type that a specific legislative requirement that an entity must do something, usually in a specific way, and that auditors must specifically report using a separate audit report that it has been done. It's more than the broad legislative compliance component of a financial or annual audit requirement.

Compliance audit should be conducted in accordance with ISSAI, formal audit criteria such as laws, normative acts, ministerial directives or the terms of an agreement or contract and/ or informal like the Code of Conduct or good governance principles.

Compliance audit is an independent activity stating whether the system, operations and processes of public sector entities audited are in accordance with laws, regulations and authorities that govern them and that these are “fit for purpose.”

There will be various audits that arise that might be a bit different to others, and in these cases going back to the key components of shaping a sound and robustly planned and executed audit is critical.

It should be noted that different jurisdictions may use different types of audit to capture areas to be audited, i.e. by compliance audit standards or performance audit standards. For example in some jurisdictions they don't consider work done as an investigation or inquiry to be a compliance audit, although there may be some assessment of compliance with legislations as part of that work but the related term of reference and conclusions are usually much wider. In deciding with such situation, SAI should be clear on what and why a type of audit is to be used for that specific type of audit. For performance audit, refer to the Performance Audit Manual for guidance.

5.2 One-off Compliance Audits

They will usually arise as the result of a request from government or Parliament and frequently as the result of a “crisis”.

They are also often termed “Special Investigations”. Their distinguishing feature is that they cannot be programmed into the audit plan as they arise because of an actual or perceived problem.

These will usually be undertaken on major systems or projects. Most SAI will not plan for such audits – preferring to include such audits as part of the process of supporting the development of the audit opinion on the Annual Financial Statements rather than as a separate audit.

However, it would be prudent to either budget a block of time for any such audits the need for which becomes apparent during the year or use time from the “reserve” to cover them. If resources are not available, the SAI should request additional funding in order to accede to the audit request.

For example, if it becomes apparent that there is a large loss of revenue, a compliance audit can be undertaken to determine whether the system was badly designed in the first place or other reason why malfeasance was possible. This work is in addition to the normal systems review work which forms part of the audit of AFS (see [4.3.10 above](#)).

It is essential that such audits have an Engagement Letter detailing precisely what is expected from the audit (see [Annex 15](#)).

Also see the **Case Study** which provides an example – for procurement – of identifying good international practice and undertaking a major compliance audit.

5.3 Performance Audits

Compliance audits will usually form part of a Performance Audit (PA); indeed, most PA will contain multiple compliance audits to confirm that adequate systems exist – and are being followed – as part of the overall audit of economy, efficiency, effectiveness and equity.

For example, a PA of whether or not a government’s health policy is being implemented in the best possible way might include compliance audits covering:

- **Approved Pharmaceuticals:** is there an adequate system of approved pharmaceuticals and a system for adding new items to the list;
- **Pharmaceutical Procurement Plan:** does one exist and, if so, was it complied with;
- **Pharmaceutical Purchasing:** did purchases comply with the purchasing regulations;
- **Storage and Issuing of Pharmaceuticals:** were all aspects of the Stores Manual complied with regards recording delivery, storage and issuing of pharmaceuticals; and
- **Usage of Pharmaceuticals:** was the system for recording the use of pharmaceuticals and its feed back into the planning process complied with?

Every PA will involve looking at a variety of interlocking systems and determining the extent to which they have been complied with.

Please see the Performance Audit Manual for details of performance auditing and compliance auditing’s place therein.

5.4 Budget Audits

The audit of the budget prior to its presentation to Parliament is still relatively rare but is an area which SAI should be striving to get powers so to do. Such reports can be regarded as “Stand Alone Compliance Audits” as they should seek to identify the extent to which

the government has complied with its own rules and regulations during the budgetary preparation process.

The goal here is to audit the draft budget to ensure that it has been compiled on the basis of past results and reasonable assumptions about the future. These would include realistic estimates of world economic trends including prices for import and export commodities. They also include internal factors such as demography and its effects of government spending (more young people requiring education; more elderly people requiring health care) and revenue (the numbers in the working age bands).

The Ministry of Finance should have detailed regulations as to how it should compile the budget and the audit will be to ensure that it has complied with this.

At the same time, a systematic analysis of the formation of the parameters of the draft budget and their compliance with the priorities of socio-economic development is carried out.

The SAI should be actively involved in the systematic, unprejudiced assessment of the risks associated with forecasting, planning and ongoing use of national resources, in terms of the long-term interests of social development. This will help avoid the so-called “institutional traps,” where decisions that seem effective in the short term can bring about expenditure of irreplaceable resources and strategic defeat to the community and the state in the future.

It is necessary to build systematic work to ensure integrated and comprehensive audit (control) of budget expenditures taking into account their volumes and social significance.

The compliance audit reports of the SAI should be based on the following estimates:

- assessment of the use of budget resources in the context of legality, effectiveness and efficiency; and
- assessment of the budget system, taking into account the dynamics of the total external debt of the country.

Attention will be paid to the quality of the audit of the state budget, as well as the use of modern methods of assessing risks to the stability of the budget system.

5.5 Donor Funded Projects

There is a danger that projects paid for, or financially supported, from foreign aid funds will be accorded less attention by audit offices (as well as by government officials) because of the apparent limited impact on the country’s own resources.

In practice, there are good reasons for close scrutiny of aid funding:

- invariably development projects tie up a country’s resources (accommodation, staff) which might be better used in other ways;
- there are often substantial domestic costs implications in terms of support services and future running costs (maintenance, spare parts, training, interest charges) which will not be aid funded;
- there is a danger that the effects on the balance of payments will be overlooked; and
- if projects are identified by *ad hoc* arrangements, financial inputs can be side-tracked away from more essential tasks.

Donor-funded projects are programmes designed to promote sustainable development for the recipient countries. These economic development and humanitarian assistance

programmes can generally be grouped into six major categories, viz.

- promoting broad-based economic growth;
- advancing democracy;
- stabilising population and protecting human health;
- protecting the environment;
- building human capacity through education and training; and
- saving lives and preventing disasters through humanitarian assistance.

Donor funds are very important to developing countries, as they need the funds for the implementation of economic development, environmental protection and human capacity building programmes, which cannot be accommodated by their limited internal economic resources.

Donor agreements with foreign recipients require them to contract independent auditors of the funds provided under the agreements. However, these audits should be performed with the applicable INOTOSAI guidelines. The importance of SAI's involvement in the audit of donor-funded projects cannot be overemphasised. Any money and or materials given to any government agency in any country by a donor belongs to the government of that country. Therefore, SAI are expected to, and should be involved in the audit of such donor funds since the funds are part of the financial statement of the government.

The two major types of donor-funding are bilateral and multilateral funding. Bilateral funding is a situation whereby a foreign donor agency of one country provides funds and or materials directly to an agency in the receiving country for the implementation of economic development, environmental protection or human capacity building, etc. in the receiving country (e.g. DfID; SIDA; CIDA; USAID; AusAID; etc.)

Multilateral funding is on the hand, a situation whereby the donor is a grouping of foreign countries which pay money into a common pool for use in development (e.g. the World Bank; the European Commission; the Asian Development Bank etc.)

Although different donors use different implementation and reporting guidelines and require different financial statements, the accounting system of a donor-funded Project should follow clearly documented accounting standards. Regardless of the type of project, sector involved or means of disbursing funds, it is important that the project organisation maintain adequate and clear accounting records of all expenditures. The preparation of the financial report is the responsibility of project management or government officials.

A number of SAI in the region have encountered problems in auditing donor funded projects due to the following;

- Most government departments receive funds from different donors. Different donors have different accountability requirements. It takes a lot of resources and expertise for both management and audit to respond to the differing requirements. As a result, some SAI request donors with specific elaborate requirements to have their projects audited by private chartered accountancy firms;
- In some cases, the recipients have not been trained on donor specific requirements resulting in delays in reporting;
- Audit clauses are sometimes included in aid agreements without the knowledge of the SAI. This results in SAI having to undertake audit work which has not been adequately planned for;
- Some SAI lack of financial resources to carry out full audits especially where donor

projects are scattered throughout the country;

- Some Governments in the region do not have integrated financial management and control systems. This makes extraction of donor specific information cumbersome; and
- Absence of supporting documents, especially where donor accounting is outside the Treasury centralised accounting system.

There is need for SAI to carry on continuous dialogue with Donors and their Governments to counter the above problems.

See [Annex 16](#) for a detailed description of how to undertake these audits.

5.6 Social Responsibility Audits

5.6.1 Introduction

This is another area which is still relatively rare but which will become of increasing importance to regional SAIs. This section outlines some of these topics but SAIs will need to ensure that they keep abreast of new developments. PASAI will be able to advise regional SAIs on such developments.

Examples of Social Responsibility Audits include:

- **Gender Audit:** ensuring equity of government expenditure by gender;
- **Environmental Audit (including Climate Change):** ensuring that the government has a realistic policy which it is implementing; and
- **Pandemic/Epidemic Audit:** ensuring that the government has stockpiles of equipment and a plan for dealing with such outbreaks.

5.6.2 Gender Audit

Gender sensitivity has been adopted as one of the critical strategies to promote equality in the development process. Being gender sensitive means approaching life with a gender perspective, being aware that every development action taken will affect women as well as men differently, and making a conscious move to ensure that men as well as women have the same access to and opportunity for development. In an attempt to achieve equal access and opportunities, the United Nations family has pledged to mainstream gender in all development activities. This pledge is embodied in their Platform for Action, to which governments of the world are signatories. Paragraph 79 of the Platform for action reads:

“Governments and other actors should promote an active and visible policy of mainstreaming a gender perspective into all policies and programmes, so that, before decisions are taken, an analysis is made of the effects on women and men, respectively.”

Gender refers to the social construction of the roles played by women and men in society. This perception of the differences between women and men starts at birth, where different societies already give differential treatment to the new-born girl or boy. It is very important to note that how these two are treated will differ from one society to another. However, in most cases the effect of the difference is that boys and girls are, from an early age, moulded and nurtured for different adulthood roles. These roles are therefore anticipated and are reinforced by society throughout one’s life.

Men and women play different roles. The analysis of roles women play is as follows:

- **Reproductive Role:** referring to the reproduction of human beings, their care and

maintenance – in the household. This would include preparing food, getting water, and taking care of all their subsistence needs. This is the work that is not valued in financial terms and is often referred to as just “women’s work”;

- **Productive Role:** participation in paid work outside the household - production of services or food crops, work in factories, in the offices, etc.; and
- **Community Role:** activities that are usually the extension of the reproductive role - various activities that contribute to the upkeep/maintenance of the community - taking care of the sick, the children, building of roads, wells, social events, etc.

Gender analysis is a systematic way in which we explore how gender affects the participation of men and women in any development process. Gender analysis applies a tool or framework to examine what men and women do and what resources, for example, time, money, etc. are at their disposal to do what they have to do.

Through a gender analysis it is hoped that imbalances in the allocation of resources will be revealed and that resources can be appropriately distributed to ensure equality among men and women. Gender analysis is a methodology that aims to:

- Identify and understand the differences in the lives of women and men, and the diversity among women themselves;
- Assess how policies, programmes or projects may impact differently on women and men, girls and boys;
- Compare how and why women and men are affected differently through the collection and utilisation of sex-disaggregated data, both qualitative and quantitative; and
- Integrate gender considerations throughout the planning, design, implementation and evaluation process.

It is important to analyse everything with a gender eye because of:

- The division of labour per sex, which breeds inequality and discrimination between the two sexes;
- Unequal access to and control over resources between women and men;
- Unequal access to and control over opportunities between women and men;
- Unequal access to participation in development activities; and
- Unequal access to and control over power.

Auditing plays a very critical role in ensuring that there is accountability for public funds. At the very **heart of public expenditure is the promotion of human development**, and hence it is important that there are vehicles to ensure that those responsible for public resources do indeed account for them.

Human development as defined by the UNDP (1995) is the expansion of choices available to people - women as well as men. The choices are categorised as follows:

- **Essential Choices:** long and healthy life, acquisition of knowledge, access to resources needed for decent life;
- **Additional Choices:** political, economic and social freedom to grasp opportunities for being creative and productive.

Human development also involves four critical pillars:

- **Productivity:** meaning full participation in the productive sector;
- **Equity:** access to equal opportunity;
- **Sustainability:** in terms of access to opportunities; and

- **Empowerment:** meaning full participation in the decisions and processes of development.

The above ethos for human development sets a **very firm and specific direction for gender awareness in auditing**. First, it says all people – women and men, should have equal chances to expand their choices. Secondly, it says that for human (women and men) development to be achieved, the elements of productivity, equity, sustainability and empowerment have to be upheld. Any development intervention should therefore be assessed/evaluated in terms of its achievement of the above pillars.

Gender awareness in auditing means that an auditor is using gender lenses to assess how public funds have been expended to promote human development. Gender awareness in auditing is also concerned with equality, equity and empowerment of women and men in the development process. The critical question being asked is:

“How responsible has a particular expenditure been in terms of promoting the development of women as well as men?”

Gender issues need to be considered throughout the audit process. Steps in the audit process should be approached bearing in mind that:

- Women and men have special needs; therefore, the auditing process should look out for this;
- In our societies women have been mostly disadvantaged, so interventions should take this into consideration; and
- Human development is about expanding the choices of both women and men, bearing in mind productivity, equity, sustainability and empowerment.

The SAI, as the custodian of public resources, have the responsibility to ensure that there are gender awareness and gender sensitivity in public spending and public accountability. This essentially means that auditors should cultivate and practise gender awareness in the audit process and practice, for example:

- **Planning:** with a gender eye and mind;
- **Execution:** with a gender hand; and
- **Reporting:** with gender facts.

How can auditors ensure that the above process becomes a reality? The first step is **gender mainstreaming** and this has been spearheaded by the United Nations body and adopted and endorsed by the SDCC family.

Mainstreaming is the process of **integrating gender equality, gender equity and gender empowerment into the development process**. It is the process that ensures that policies, the implementation of policies through **budgeting and allocation of resources**, and finally the **process issues**, have taken account of **equal involvement of men and women**. In other words, the entire development process should proceed from a premise of how it will affect women as well as men, because of their different needs, interests and priorities.

Gender awareness in auditing should therefore be a **holistic process**, looking not only at the end process of the development process or intervention. Gender awareness in auditing should **start by looking at policies and their implementation** to ensure that the gender perspective has been incorporated - that gender has been mainstreamed.

5.6.3 Environmental Audit

Given the delicate infrastructure of all PASAI members, including both Australia (bush fires

and coral reef bleaching) and New Zealand, this is a vital topic. For most members, climate change and the associated rise in sea levels, are a very serious matter – especially for the low-laying atolls. Even in the “high islands”, the majority of people live around the coastline and will be affected by rising sea levels.

Environmental Auditing relates to audits of an organisation’s activities with an environmental perspective. The growing global awareness of environmental issues in the past 30 years has among other changes led to:

- the expansion of environmental regulation by state and local authorities;
- the increasing cost of environmental protection for both the private and public sectors; and
- Governments and corporations around the world have shown more concern about sustainable development.

The following key areas of concern for environmental auditing have been identified:

- Climate Change (Global Warming and Sea Level rise)
- Fresh water conservation;
- Unsustainable utilisation of forests or deforestation;
- Wildlife park management;
- Urban pollution and sanitation; and
- Management of International Accords

An expectation has grown that those environment issues and reports should be subject to independent audit. To develop its response to the subject INTOSAI established a Working Group which was responsible for developing guidelines and methodologies for the conduct of environmental audits and the development of technical criteria by SAI.

This section attempts to summarise the guidance developed by the INTOSAI Working Group on Environmental Auditing. At the XV INCOSAI (Cairo), it was agreed that the environmental auditing is in principle not different from the audit approach as practiced by SAI and it could encompass all types of audits. SAI should to the full extent appropriate take the INTOSAI Auditing Standards into account when planning, conducting and reporting on an environmental audit.

The **scope** of an environmental audit varies. It can be comprehensive, take on a range of issues or address a single topic. Environmental issues are encountered at different levels and in different forms. Most environmental issues have trans-boundary character for example global problems like global warming, acid rain and ocean pollution. This has led to a number of international agreements agreed to by countries depending on the issue.

At the national level, most countries have got national policies relating to the environment, which are supported by various regulations. The national policies usually identify a responsible ministry or agency to be responsible for supervision and ensuring proper policy implementation. Public and private sector organisations are responsible for implementation of policy.

Environmental audits can take the form of **Regularity (Financial and Compliance)** and **Performance Audits**. The objective of a regularity audit on environment aspects will be to establish whether the reporting entity has appropriately recognised, valued and reported environmental costs, liabilities and assets and whether the entity has conducted the environmental activity in compliance with all applicable obligations.

A performance audit will enable the auditor to establish whether the entity has conducted the environmental activity in an effective, efficient, economical and equitable manner consistent with the applicable government policy.

INTOSAI provides guidance on this topic:¹⁴

- **GUID #5200: Activities with an Environmental Perspective:** the guidance provides SAI with a basis for understanding the nature of environmental auditing as it has so far developed in the governmental sphere;
- **GUID #5201: Environmental Auditing in the Context of Financial and Compliance Audits:** provides guidance on how to conduct environmental audits by applying financial and compliance audit practices;
- **GUID #5202: Sustainable Development: the Role of the SAI:** an overview of the concept of sustainable development and includes practical guidance to SAI on how to integrate sustainable development into their audit planning;
- **GUID #5203: Co-operation on Audits of International Environmental Accords:** outlines the approaches by which the audits of environmental accords might be carried out and describes ways of co-operation between SAI.

5.6.4 Pandemic/Epidemic Audit

Given that the coronavirus COVID-19 is devastating the planet at the time of drafting, this is a very pertinent topic. However, it does not require a pandemic to be a pertinent audit topic as the recent measles epidemic in Samoa sadly illustrates.

Whilst no government could have been prepared for the scale of the coronavirus, there should be in place plans for dealing with epidemics/pandemics should they arise.

Staff of SAI are not medically qualified but it is still possible for the SAI to play a key role in ensuring that a country is ready for any future epidemic/pandemic,

The audit process here is to ensure that such plans exist and that they are reasonable in comparison with those of other similar countries. For example, the availability or stockpiling of items such Personal Protective Equipment (PPE) (gowns, masks, visors, etc.), Intensive Care Equipment (ICE) (ventilators) and vaccines (where these exists) should be ensured.

Also, the plans should be tested and updated on a regular basis.

The sort of thing we would expect to see include:

1: Education and Prevention

One of the most important components of pandemic preparedness is ensuring that employees are educated on the facts and that the government is prepared to enforce strategies for avoiding the spread of the disease that has infected the employee base. Proper hygiene and encouraging sick personnel to remain at home are at the top the list of prevention tactics and should be initiated during a potential pandemic outbreak.

2: Cross Training

Ensuring that key functions can be performed in the absence of essential personnel is necessary for the successful continuance of operations. Cross training processes protects against single points of failure in knowledge in the event that the only person trained to perform a task is unavailable.

3: Remote Capabilities

Planning for personnel to work from home can be an option during a pandemic episode. However, it is important that this recovery solution is thoroughly tested to ensure its viability. A couple of important questions to ask when planning for a remote solution are:

- Do users have the appropriate tools to work successfully from home?
- Is there enough bandwidth to adequately support the number of remote users that may be necessary during different situations?

4: Critical Suppliers

It is also important to remember that a pandemic outbreak could be widespread and not just affect a single business – third party providers that are depended on for goods and services could also be affected. Therefore, incorporating backup plans for key suppliers must be a part of planning.

5: Communication

If personnel cannot go on-site for long periods of time, does the government have an effective plan in place to sustain ongoing communications to remote users? It is necessary to ensure that important information can be exchanged so employees are kept abreast of any developments or changes in requirements as the situation progresses.

Ensuring that your government has incorporated these focus areas into its planning will help increase its preparedness to respond to a pandemic.

Apart from ensuring the existence of a plan. The SAI should play a key role in monitoring government expenditure with regards the pandemic. Of its nature, huge sums of money will be spent with far less due process and control than in normal circumstances. This give a lot of scope for inefficiency and fraud. In the UK, crooks have set up companies pretending to be able to supply PPE to the government and other are claiming 80% of staff wages for non-existent or non-furloughed staff.

The SAI will need to be highly innovative and flexible in its attempts to ensure that as much government money as possible is actually used to alleviate the health and economic problems caused by this pandemic and any similar future events.

The former ISSAI #5510 to #5540 provided guidance on various aspects Disaster Relief Auditing. Although no longer standards, they do contain useful material for SAI to which reference should be made.

Chapter 6: Compliance Auditing Under the Judicial Approach

The key points are: [Introduction](#); [Performing Audits in a Court of Accounts](#); [Communicating and Enforcing the Law](#); and [Processes in Various Models of Courts of Accounts](#).

6.1 Introduction

This Chapter examines the “Additional Guidance” provided for Public Sector Auditors operating in a Court of Accounts (Judicial) Environment. Such SAIs have the power to exercise judgments and decisions over the accounts and over responsible persons, including accountants and administrators (ISSAI #100, 1.0.21).

The precise way of undertaking Compliance Audits will depend on the individual jurisdiction but this general standard should be followed (see 6.4 below for examples).

This guidance was originally part of the former ISSAI #4100 (section #10) but was subsequently hived-off to become a new draft ISSAI #4300 prior to the introduction of the new standards.

6.2 Performing Audits in a Court of Accounts

When performing compliance audits of individual public accounts or of the general state budget, public sector auditors in a Court of Accounts environment also:

- Obtain reasonable assurance about whether the information presented in the individual public accounts and the underlying transactions are in compliance, in all material respects, with the authorities that govern them;
- Determine whether the execution of the state budget has been carried out in compliance, in all material respects, with the authorities governing it and with individual public accounts; and
- Report the findings to the appropriate parties.

The unique jurisdictional status described above may also give rise to the need for additional considerations by public sector auditors operating in a Court of Accounts environment when planning and performing compliance audits. Such matters may include:

- Identifying the person(s) who may be held responsible for acts of noncompliance due to the potential legal implications the SAI’s judgment may have on such persons. Public officials may be held personally liable for the loss or waste of public funds, requiring them to repay the full amount of any such losses;
- Taking into consideration the applicable prescriptive period, the actions interrupting prescription of personal liability and the exact time period for which public officials may be held liable;
- Distinguishing personal liability for acts of non-compliance from the liability for unlawful acts (suspected fraud). For unlawful acts there may be a need to perform additional audit procedures;
- Liaising with prosecutors and police as appropriate in understanding the audited entity and its environment, assessing risks of non-compliance, dealing with instances of non-compliance that may indicate fraud, and reporting on such matters;
- Considering the need for addition at levels of, or more formalised procedures for quality control;

- Performing inquiry in written form (as opposed to orally);
- Ensuring that audit documentation complies with relevant rules of evidence;
- Communicating in a highly formalised manner;
- Including in the report the explicit criteria against which public officials may be held liable, including any amounts likely to be involved; and
- Considering the most appropriate form of conclusions, including recommendations, identification of damages, or court orders that may lead to a formal discharge of responsibility or to a formal determination of liability.

6.3 Communicating and Enforcing the Law

Public sector auditors in Court SAs also communicate compliance issues that may result in legal action, damages or prosecution for a criminal offence to the judge, attorney or section responsible for dealing with judgment issues within the Court, or to other bodies as appropriate. In addition, Court SAs may also communicate remarks of a more general, or informative nature resulting from the audit work to appropriate officials of the audited entity.

When enforcing the law regarding public officials, decisions taken by Court SAs are subject to:

- Due process of law and public hearing;
- Public disclosure;
- Communication to appropriate law enforcement authorities when there is evidence of a criminal offence.

6.4 Processes in Various Models of Courts of Accounts

For SAs operating in a Court of Accounts environment, the work performed may involve various phases including audit, instruction and formal judgment.

Some SAs operating in a Court of Accounts environment follow the audit process as it is described in these guidelines. However, following the planning, performance and evidence gathering phases, there may then be additional and specific issues that may lead to opening the process of instruction and to a final formal judgment.

In the event a judge or attorney decides on instructing a case, the objective of instruction is to gather enough evidence on the guilt or innocence of the public official who allegedly caused a damage, so as to allow a judgment to be made.

In some SAs operating in a Court of Accounts environment, the auditors may also act in the role of judges and may be empowered to both audit and give formal judgments. In these cases, the instruction phase is an integral part of the audit planning, performance and evidence gathering phases, such that the audit is planned with a view to covering all these phases.

Chapter 7: Compliance Auditing under Auditing Standards Board Standard #117

This chapter looks at: [Overview](#); [Introduction and Applicability](#); [Management's Responsibilities](#); [Objectives](#); [Establish Materiality Levels](#); [Identifying Government Programs and Applicable Competence Requirements](#); [Performing Risk Assessment Procedures](#); [Assessing the Risk of Material Noncompliance](#); [Performing Further Audit Procedures in Response to Assessed Risks](#); [Supplementary Audit Requirements](#); [Written Representations](#); [Subsequent Events](#); [Evaluating the Sufficiency and Appropriateness of the Audit Evidence and Forming an Opinion](#); [Reporting](#); [Documentation](#); [Reissuance of a Compliance Report](#); and [Exhibit](#).

7.1 Overview

The Government Auditing Standards (the “Yellow Book”) of the General Accounting Office has a chapter (#7) covering “**Standards for Attestation Engagements and Reviews of Financial Statements**”. This covers aspects of Compliance Audits and should be read in conjunction with the material below.

Statement on Auditing Standards #117, “**Compliance Audits**” which the Auditing Standards Board has issued in AU section 801 of AICPA *Professional Standards* to:

- reflect changes in the compliance audit environment and incorporate the risk assessment standards;
- require the auditor to adapt and apply the AU sections of AICPA *Professional Standards* to a compliance audit and provides guidance on how to do so; and
- identify the AU sections that are not applicable to a compliance audit, define terms related to compliance audits and used in the SAS, and identify the elements to be included in an auditor’s report on a compliance audit.

The remainder of this chapter examine **Section #801** but, as ever, this is no substitute for reading the original document. The numbers at the start of individual paragraphs are those in AU #801.

The techniques used to undertake the actual compliance audit work are the standards one examined in the next chapter.

7.2 Introduction and Applicability

01. Governments frequently establish governmental audit requirements for entities to undergo an audit of their compliance with applicable compliance requirements. This section is applicable when an auditor is engaged, or required by law or regulation, to perform a compliance audit in accordance with all of the following:

- Generally Accepted Auditing Standards (GAAS);
- The standards for financial audits under *Government Auditing Standards*; and
- A governmental audit requirement that requires an auditor to express an opinion on compliance.

An example of an engagement to which this section is applicable is an audit performed in accordance with the provisions of Office of Management and Budget (OMB) Circular A-133, Audits of States, Local Governments and Non-Profit Organizations.

Another example is a department specific requirement such as the U.S. Department of Housing and Urban Development Audit Requirements Related to Entities Such As Public

Housing Agencies, Non-profit and For-Profit Housing Projects, and Certain Lenders.

02. This section addresses the application of GAAS to a compliance audit. Compliance audits usually are performed in conjunction with a financial statement audit. This section does not apply to the financial statement audit component of such engagements.

7.3 Management's Responsibilities

08. A compliance audit is based on the premise that management is responsible for the entity's compliance with compliance requirements. Management's responsibility for the entity's compliance with compliance requirements includes the following:

- a.* Identifying the entity's government programs and understanding and complying with the compliance requirements
- b.* Establishing and maintaining effective controls that provide reasonable assurance that the entity administers government programs in compliance with the compliance requirements
- c.* Evaluating and monitoring the entity's compliance with the compliance requirements
- d.* Taking corrective action when instances of noncompliance are identified, including corrective action on audit findings of the compliance audit

7.4 Objectives

10. The auditor's objectives in a compliance audit are to:

- a.* obtain sufficient appropriate audit evidence to form an opinion and report at the level specified in the governmental audit requirement on whether the entity complied in all material respects with the applicable compliance requirements; and
- b.* identify audit and reporting requirements specified in the governmental audit requirement that are supplementary to GAAS and Government Auditing Standards, if any, and perform procedures to address those requirements.

Most governmental audit requirements specify that the auditor's opinion on compliance is at the program level. However, some governmental audit requirements may specify a different level (for example, at the applicable compliance requirement level).

Governmental audit requirements also may set forth specific supplementary requirements of the compliance audit (for example, procedures to be performed by the auditor, documentation requirements, the form of reporting, and continuing professional education requirements with which the auditor is required to comply).

7.5 Establish Materiality Levels

13. The auditor should establish and apply materiality levels for the compliance audit based on the governmental audit requirement.

In a compliance audit, the auditor's purpose for establishing materiality levels is to

- a.* determine the nature and extent of risk assessment procedures;
- b.* identify and assess the risks of material noncompliance;
- c.* determine the nature, timing, and extent of further audit procedures;

- d. evaluate whether the entity complied with the applicable compliance requirements; and
- e. report findings of noncompliance and other matters required to be reported by the governmental audit requirement.

Generally, for all of the purposes identified above, the auditor's consideration of materiality is in relation to the government program taken as a whole. However, the governmental audit requirement may specify a different level of materiality for one or more of these purposes.

As the governmental audit requirement usually is established by the grantors and the auditor's report on compliance is primarily for their use, the auditor's determination of materiality usually is influenced by the needs of the grantors. However, in a compliance audit, the auditor's judgment about matters that are material to users of the auditor's report also is based on consideration of the needs of users as a group, including grantors.

7.6 Identifying Government Programs and Applicable Competence Requirements

14. As discussed above, a compliance audit is based on the premise that management is responsible for identifying the entity's government programs and understanding and complying with the compliance requirements. The auditor should determine which of those government programs and compliance requirements to test (that is, the applicable compliance requirements) in accordance with the governmental audit requirement.

Some governmental audit requirements specifically identify the applicable compliance requirements. Other governmental audit requirements provide a framework for the auditor to determine the applicable compliance requirements.

The following are some of the sources an auditor may consult when identifying and obtaining an understanding of the applicable compliance requirements:

- a. The *Compliance Supplement*, which is issued by OMB, and used in OMB Circular A-133 audits, contains the compliance requirements that typically are applicable to federal government programs, as well as suggested audit procedures when compliance requirements are applicable and have a direct and material effect on the entity's compliance. Part 7 of the *Compliance Supplement* provides guidance for identifying compliance requirements for programs not included therein; and
- b. The applicable program-specific audit guide issued by the grantor agency, which contains the compliance requirements pertaining to the government program and suggested audit procedures to test for compliance with the applicable compliance requirements.

The following are procedures the auditor may perform to identify and obtain an understanding of the applicable compliance requirements if the *Compliance Supplement* or a program-specific audit guide is not applicable:

- a. Reading laws, regulations, rules, and provisions of contracts or grant agreements that pertain to the government programme;
- b. Making inquiries of management and other knowledgeable entity personnel (for example, the chief financial officer, internal auditors, legal counsel, compliance officers, or grant or contract administrators);

- c. Making inquiries of appropriate individuals outside the entity, such as
 - i. the office of the federal, state, or local program official or auditor, or other appropriate audit oversight organisations or regulators, about the laws and regulations applicable to entities within their jurisdiction, including statutes and uniform reporting requirements; and
 - ii. a third-party specialist, such as an attorney;
- d. Reading the minutes of meetings of the governing board of the entity being audited;
- e. Reading audit documentation about the applicable compliance requirements prepared during prior years' audits or other engagements; and
- f. Discussing the applicable compliance requirements with auditors who performed prior years' audits or other engagements.

The procedures listed in this section also may assist the auditor in obtaining a further understanding of the applicable compliance requirements even when the *Compliance Supplement* or program-specific audit guide is applicable.

7.7 Performing Risk Assessment Procedures

15. For each of the government programs and applicable compliance requirements selected for testing, the auditor should perform risk assessment procedures to obtain a sufficient understanding of the applicable compliance requirements and the entity's internal control over compliance with the applicable compliance requirements.

16. In performing risk assessment procedures, the auditor should inquire of management about whether there are findings and recommendations in reports or other written communications resulting from previous audits, attestation engagements, and internal or external monitoring that directly relate to the objectives of the compliance audit. The auditor should gain an understanding of management's response to findings and recommendations that could have a material effect on the entity's compliance with the applicable compliance requirements (for example, taking corrective action). The auditor should use this information to assess risk and determine the nature, timing, and extent of the audit procedures for the compliance audit, including determining the extent to which testing the implementation of any corrective actions is applicable to the audit objectives.

Obtaining an understanding of the government program, the applicable compliance requirements, and the entity's internal control over compliance establishes a frame of reference within which the auditor plans the compliance audit and exercises professional judgment about assessing risks of material noncompliance and responding to those risks throughout the compliance audit.

The nature and extent of the risk assessment procedures the auditor performs may vary from entity to entity and are influenced by factors such as the following:

- The newness and complexity of the applicable compliance requirements;
- The auditor's knowledge of the entity's internal control over compliance with the applicable compliance requirements obtained in previous audits or other professional engagements;
- The nature of the applicable compliance requirements;
- The services provided by the entity and how they are affected by external factors

- The level of oversight by the grantor or pass-through entity; and
- How management addresses findings.

Performing risk assessment procedures to obtain an understanding of the entity's internal control over compliance includes an evaluation of the design of controls and whether the controls have been implemented. Internal control consists of the following five interrelated components: the control environment, the entity's risk assessment, information and communication systems, control activities, and monitoring.

The auditor's procedures described in paragraph 16 above, related to understanding how management has responded to findings and recommendations that could have a material effect on the entity's compliance with the applicable compliance requirements, are performed to assist the auditor in understanding whether management responded appropriately to such findings. Examples of external monitoring include regulatory reviews, program reviews by government agencies or pass-through entities, and grantor reviews. Examples of internal monitoring include reports prepared by the internal audit function and internal quality assessments.

7.8 Assessing the Risk of Material Noncompliance

17. The auditor should assess the risks of material noncompliance whether due to fraud or error for each applicable compliance requirement and should consider whether any of those risks are pervasive to the entity's compliance because they may affect the entity's compliance with many compliance requirements.

Factors the auditor may consider in assessing the risks of material noncompliance are as follows:

- The complexity of the applicable compliance requirements;
- The susceptibility of the applicable compliance requirements to non-compliance;
- The length of time the entity has been subject to the applicable compliance requirements;
- The auditor's observations about how the entity has complied with the applicable compliance requirements in prior years;
- The potential effect on the entity of noncompliance with the applicable compliance requirements;
- The degree of judgment involved in adhering to the compliance requirements; and
- The auditor's assessment of the risks of material misstatement in the financial statement audit

In assessing the risks of material noncompliance, the auditor may evaluate inherent risk of noncompliance and control risk of noncompliance individually or in combination.

Examples of situations in which there may be a risk of material noncompliance that is pervasive to the entity's noncompliance are as follows:

- An entity that is experiencing financial difficulty and for which there is an increased risk that grant funds will be diverted for unauthorised purposes; and
- An entity that has a history of poor record keeping for its government programs

7.9 Performing Further Audit Procedures in Response to Assessed Risks

18. If the auditor identifies risks of material noncompliance that are pervasive to the entity's compliance, the auditor should develop an overall response to such risks.

19. The auditor should design and perform further audit procedures, including tests of details (which may include tests of transactions) to obtain sufficient appropriate audit evidence about the entity's compliance with each of the applicable compliance requirements in response to the assessed risks of material noncompliance. Risk assessment procedures, tests of controls, and analytical procedures alone are not sufficient to address a risk of material noncompliance.

A compliance audit includes designing procedures to detect both intentional and unintentional material noncompliance. The auditor can obtain reasonable, but not absolute, assurance about the entity's compliance because of factors such as the need for judgment, the use of sampling, the inherent limitations of internal control over compliance with applicable compliance requirements, and the fact that much of the evidence available to the auditor is persuasive rather than conclusive in nature. Also, procedures that are effective for detecting noncompliance that is unintentional may be ineffective for detecting noncompliance that is intentional and concealed through collusion between entity personnel and a third party or among management or employees of the entity. Therefore, the subsequent discovery that material noncompliance with applicable compliance requirements exists does not, in and of itself, evidence inadequate planning, performance, or judgment on the part of the auditor.

An auditor may decide to use audit sampling to obtain sufficient appropriate audit evidence in a compliance audit.

To test for compliance with applicable laws and regulations, tests of details (including tests of transactions) may be performed in the following areas:

- Grant disbursements or expenditures;
- Eligibility files;
- Cost allocation plans; and
- Periodic reports filed with grantor agencies.

The use of analytical procedures to gather substantive evidence is generally less effective in a compliance audit than it is in a financial statement audit. However, substantive analytical procedures may contribute some evidence when performed in addition to tests of transactions and other auditing procedures necessary to provide the auditor with sufficient appropriate audit evidence.

20. The auditor should design and perform further audit procedures in response to the assessed risks of material noncompliance. These procedures should include performing tests of controls over compliance if:

- the auditor's risk assessment includes an expectation of the operating effectiveness of controls over compliance related to the applicable compliance requirements;
- substantive procedures alone do not provide sufficient appropriate audit evidence; or
- such tests of controls over compliance are required by the governmental audit requirement.

If any of the conditions in this paragraph are met, the auditor should test the operating effectiveness of controls over each applicable compliance requirement to which the conditions apply in each compliance audit.

7.10 Supplementary Audit Requirements

21. The auditor should determine whether audit requirements are specified in the governmental audit requirement that are supplementary to GAAS and *Government Auditing Standards* and perform procedures to address those requirements, if any.

22. In instances where audit guidance provided by a governmental agency for the performance of compliance audits has not been updated for, or otherwise conflicts with, current GAAS or *Government Auditing Standards*, the auditor should comply with the most current applicable GAAS and *Government Auditing Standards* instead of the outdated or conflicting guidance.

Examples of supplementary audit requirements are the requirements in OMB Circular A-133 for the auditor to:

- perform specified procedures to identify major programs.
- follow up on prior audit findings and perform procedures to assess the reasonableness of the summary schedule of prior audit findings.

When there is conflicting guidance, the auditor may decide to consult with the government agency responsible for establishing audit guidance or that provides the funding.

7.11 Written Representations

23. The auditor should request from management written representations that are tailored to the entity and the governmental audit requirement:

- a. acknowledging management's responsibility for understanding and complying with the compliance requirements;
- b. acknowledging management's responsibility for establishing and maintaining controls that provide reasonable assurance that the entity administers government programs in accordance with the compliance requirements;
- c. stating that management has identified and disclosed to the auditor all of its government programs and related activities subject to the governmental audit requirement;
- d. stating that management has made available to the auditor all contracts and grant agreements, including amendments, if any, and any other correspondence relevant to the programs and related activities subject to the governmental audit requirement;
- e. stating that management has disclosed to the auditor all known noncompliance with the applicable compliance requirements or stating that there was no such noncompliance;
- f. stating whether management believes that the entity has complied with the applicable compliance requirements (except for noncompliance it has disclosed to the auditor);
- g. stating that management has made available to the auditor all documentation related to compliance with the applicable compliance requirements;
- h. identifying management's interpretation of any applicable compliance requirements that are subject to varying interpretations;
- i. stating that management has disclosed to the auditor any communications from

grantors and pass-through entities concerning possible noncompliance with the applicable compliance requirements, including communications received from the end of the period covered by the compliance audit to the date of the auditor's report;

j. stating that management has disclosed to the auditor the findings received and related corrective actions taken for previous audits, attestation engagements, and internal or external monitoring that directly relate to the objectives of the compliance audit, including findings received and corrective actions taken from the end of the period covered by the compliance audit to the date of the auditor's report;

k. stating that management has disclosed to the auditor all known noncompliance with the applicable compliance requirements subsequent to the period covered by the auditor's report or stating that there were no such known instances; and

l. stating that management is responsible for taking corrective action on audit findings of the compliance audit.

24. If the auditor determines that it is necessary to obtain additional representations related to the entity's compliance with the applicable compliance requirements, the auditor should request such additional representations.

In some cases, management may include qualifying language in the written representations to the effect that representations are made to the best of management's knowledge and belief. However, such qualifying language is not appropriate for the representations in paragraphs .23(a), .23(b), and .23(l).

7.12 Subsequent Events

25. The auditor should perform audit procedures up to the date of the auditor's report to obtain sufficient appropriate audit evidence that all subsequent events related to the entity's compliance during the period covered by the auditor's report on compliance have been identified.

26. The auditor should take into account the auditor's risk assessment in determining the nature and extent of such audit procedures, which should include, but are not limited to, inquiring of management about and considering:

- relevant internal auditors' reports issued during the subsequent period;
- other auditors' reports identifying noncompliance that were issued during the subsequent period;
- reports from grantors and pass-through entities on the entity's noncompliance that were issued during the subsequent period; and
- information about the entity's noncompliance obtained through other professional engagements performed for that entity.

27. The auditor has no obligation to perform any audit procedures related to the entity's compliance during the period subsequent to the period covered by the auditor's report. However, if before the report release date, the auditor becomes aware of noncompliance in the period subsequent to the period covered by the auditor's report that is of such a nature and significance that its disclosure is needed to prevent report users from being misled, the auditor should discuss the matter with management and, if appropriate, those charged with governance, and should include an explanatory paragraph in his or her report describing the nature of the noncompliance.

Two types of subsequent events may occur. The first type consists of events that provide additional evidence with respect to conditions that existed at the end of the reporting period that affect the entity's compliance during the reporting period. The second type consists of events of noncompliance that did not exist at the end of the reporting period but arose subsequent to the reporting period.

An example of a matter of noncompliance that may occur subsequent to the period being audited but before the report release date that may warrant disclosure to prevent report users from being misled is the discovery of noncompliance in the subsequent period of such magnitude that it caused the grantor to stop funding the program.

7.13 Evaluating the Sufficiency and Appropriateness of the Audit Evidence and Forming an Opinion

28. The auditor should evaluate the sufficiency and appropriateness of the audit evidence obtained.

29. The auditor should form an opinion, at the level specified by the governmental audit requirement, on whether the entity complied in all material respects with the applicable compliance requirements, and report appropriately. In forming an opinion, the auditor should evaluate likely questioned costs, not just known questioned costs, as well as other material noncompliance that, by its nature, may not result in questioned costs.

In determining whether an entity has materially complied with the applicable compliance requirements, the auditor may consider the following factors:

- a. The frequency of noncompliance with the applicable compliance requirements identified during the compliance audit;
- b. The nature of the noncompliance with the applicable compliance requirements identified;
- c. The adequacy of the entity's system for monitoring compliance with the applicable compliance requirements and the possible effect of any noncompliance on the entity; and
- d. Whether any identified noncompliance with the applicable compliance requirements resulted in likely questioned costs that are material to the government program.

The auditor's evaluation of whether the entity materially complied with applicable compliance requirements includes consideration of noncompliance identified by the auditor, regardless of whether the entity corrected the noncompliance after the auditor brought it to management's attention.

7.14 Reporting

Report on Compliance Only

30. The auditor's report on compliance should include the following elements:

- a. A title that includes the word *independent*;
- b. Identification of the one or more government programs covered by the compliance audit or reference to a separate schedule containing that information;
- c. Identification of the applicable compliance requirements or a reference to where

they can be found;

d. Identification of the period covered by the report;

e. A statement that compliance with the applicable compliance requirements is the responsibility of the entity's management;

f. A statement that the auditor's responsibility is to express an opinion on the entity's compliance with the applicable compliance requirements based on the compliance audit;

g. A statement that the compliance audit was conducted in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, and the governmental audit requirement;

h. A statement that the compliance audit included examining, on a test basis, evidence about the entity's compliance with those requirements and performing such other procedures as the auditor considered necessary in the circumstances;

i. A statement that the auditor believes the compliance audit provides a reasonable basis for his or her opinion;

j. A statement that the compliance audit does not provide a legal determination of the entity's compliance;

k. The auditor's opinion, at the level specified by the governmental audit requirement, on whether the entity complied, in all material respects, with the applicable compliance requirements;

l. If noncompliance that results in an opinion modification is identified, a description of such noncompliance, or a reference to a description of such noncompliance in an accompanying schedule;

m. If other noncompliance that is required to be reported by the governmental audit requirement is identified (that is, noncompliance that does not result in an opinion modification), a description of such noncompliance or a reference to a description of such noncompliance in an accompanying schedule;

n. If the criteria used to evaluate compliance are:

i. established or determined by contractual agreement or regulatory provisions that are developed solely for the parties to the agreement or regulatory agency responsible for the provisions; or

ii. available only to the specified parties, a separate paragraph at the end of the report that includes (1) a statement indicating that the report is intended solely for the information and use of the specified parties (2) an identification of the specified parties to whom use is restricted, and (3) a statement that the report is not intended to be and should not be used by anyone other than the specified parties;

o. The manual or printed signature of the auditor's firm; and

p. The date of the auditor's report.

Combined Report on Compliance and Internal Control Over Compliance

31. If the governmental audit requirement requires the auditor to report on internal control over compliance and the auditor combines the auditor's report on compliance with a report on internal control over compliance, the following should be added to the report elements listed in paragraph 30:

- a. A statement that management is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, rules, and provisions of contracts or grant agreements applicable to government programs;
- b. A statement that in planning and performing the compliance audit, the auditor considered the entity's internal control over compliance with the applicable compliance requirements to determine the auditing procedures for the purpose of expressing an opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance;
- c. A statement that the auditor is not expressing an opinion on internal control over compliance;
- d. A statement that the auditor's consideration of the entity's internal control over compliance was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses in internal control over compliance;
- e. The definition of *deficiency in internal control over compliance* and *material weakness in internal control over compliance*;
- f. A description of any identified material weaknesses in internal control over compliance or a reference to an accompanying schedule containing such a description;
- g. If significant deficiencies in internal control over compliance were identified, the definition of *significant deficiency in internal control over compliance* and a description of the deficiencies or a reference to an accompanying schedule containing such a description;
- h. If no material weaknesses in internal control over compliance were identified, a statement to that effect; and
- i. The restricted use paragraph described in paragraph 30(n). The restricted use paragraph should be included in all combined reports on the entity's compliance and internal control over compliance.

A combined report on compliance and internal control over compliance is presented in the exhibit of this section ([see 7.17](#)).

Separate Report on Internal Control Over Compliance

32. If the governmental audit requirement requires the auditor to report on internal control over compliance and the auditor chooses to issue a separate report on internal control over compliance, the auditor should include in that separate report the elements in paragraph 31(a)–(i) and the following additional elements:

- a. A title that includes the word *independent*;
- b. A statement that the auditor audited the entity's compliance with applicable

compliance requirements pertaining to [*identify the government program(s) and the period audited*] and a reference to the auditor's report on compliance;

c. A statement that the compliance audit was conducted in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, and the governmental audit requirement;

d. The manual or printed signature of the auditor's firm; and

e. The date of the auditor's report.

33. The auditor should report noncompliance as well as other matters that are required to be reported by the governmental audit requirement in the manner specified by the governmental audit requirement. If the other matters required to be reported by the governmental audit requirement are not appropriate for the auditor to report on, the auditor should follow paragraph 38.

34. The auditor should modify his or her opinion on compliance in accordance with section 508, *Reports on Audited Financial Statements*, if any of the following conditions exist:

a. The compliance audit identifies noncompliance with the applicable compliance requirements that the auditor believes has a material effect on the entity's compliance; or

b. A restriction on the scope of the compliance audit.

35. The auditor should modify the report described in paragraphs 30 and 32 when the auditor makes reference to the report of another auditor as the basis, in part, for the auditor's report.

36. In the absence of a governmental audit requirement to report on internal control over compliance, the auditor should, nevertheless, communicate in writing to management and those charged with governance identified significant deficiencies and material weakness in internal control over compliance.

37. The auditor also should communicate to those charged with governance of the entity the auditor's responsibilities under GAAS, *Government Auditing Standards*, and the governmental audit requirement, an overview of the planned scope and timing of the compliance audit, and significant findings from the compliance audit.

38. Printed forms, schedules, or reports designed or adopted by government agencies with which they are to be filed sometimes contain prescribed wording. If a printed form, schedule, or report requires the auditor to make a statement that he or she has no basis to make, the auditor should accordingly reword the form, schedule, or report or attach an appropriately worded separate report.

Nothing precludes the auditor from restricting the use of any report to intended users.

If the report is a matter of public record or available for public inspection, removing personally identifiable information in the compliance audit report and findings of noncompliance will reduce the likelihood of sensitive information being disclosed (Ref: par. 30(l)-(m) and 33).

When the auditor communicates significant deficiencies or material weaknesses in internal control over compliance to management and those charged with governance, *Government Auditing Standards* also requires the auditor to obtain a response from the responsible

officials, preferably in writing, concerning their views on the findings, conclusions, and recommendations included in the auditor's report on internal control over compliance and include a copy of any written response in the auditor's report(Ref: par. 36).

If such a written response is included in a document containing the auditor's written communication to management and those charged with governance concerning identified significant deficiencies or material weaknesses in internal control over compliance, the auditor may add a paragraph to his or her written communication disclaiming an opinion on such information. Following is an example of such a paragraph:

ABC Agency's written response to the significant deficiencies [*and material weaknesses*] in internal control over compliance identified in our compliance audit was not subjected to the auditing procedures applied in the compliance audit of ABC Agency's compliance and, accordingly, we express no opinion on it (Ref: par. 36).

If the auditor is submitting a reworded form, schedule, or report or appropriately worded separate report, the auditor may include a separate communication to the agency explaining why the auditor's report was modified (Ref: par. 38).

7.15 Documentation

39. The auditor should document the risk assessment procedures performed, including those related to gaining an understanding of internal control over compliance.

40. The auditor should document his or her responses to the assessed risks of material noncompliance, the procedures performed to test compliance with the applicable compliance requirements, and the results of those procedures, including any tests of controls over compliance.

41. The auditor should document materiality levels and the basis on which they were determined.

42. The auditor should document how he or she complied with the specific governmental audit requirements that are supplementary to GAAS and *Government Auditing Standards*.

The auditor is not expected to prepare specific documentation of how the auditor adapted and applied each of the applicable AU sections to the objectives of a compliance audit. The documentation of the audit strategy, audit plan, and work performed cumulatively demonstrate whether the auditor has complied with the overall compliance auditing requirements.

7.16 Reissuance of a Compliance Report

43. If an auditor reissues his or her report, the reissued report should include an explanatory paragraph stating that the report is replacing a previously issued report and describing the reasons why the report is being reissued, and any changes from the previously issued report. If additional procedures are performed to obtain sufficient appropriate audit evidence for all of the government programs being reported on, the auditor's report date should be updated to reflect the date the auditor obtained sufficient appropriate audit evidence regarding the events that caused the auditor to perform the new procedures. If, however, additional procedures are performed to obtain sufficient appropriate audit evidence for only some of the government programs being reported on, the auditor should dual date the report with the updated report date reflecting the date the auditor obtained sufficient appropriate audit evidence regarding the government programs affected by the circumstances and referencing the government programs for which additional audit procedures have been performed.

Reissuance of an auditor-prepared document required by the governmental audit requirement that is incorporated by reference into the auditor's report is considered to be a reissuance of the report.

The following are examples of situations in which the auditor might reissue the compliance report:

- A quality control review performed by a governmental agency indicates that the auditor did not test an applicable compliance requirement; and
- The discovery subsequent to the date of the compliance report that the entity had another government program that was required to be tested.

An example of an auditor-prepared document required by a governmental audit requirement that is incorporated by reference in the auditor's report is the schedule of findings and questioned costs in a compliance audit under OMB Circular A-133.

7.17 Exhibit

Illustrative Combined Report on Compliance With Applicable Requirements and Internal Control Over Compliance - (*Unqualified Opinion on Compliance; No Material Weaknesses or Significant Deficiencies in Internal Control Over Compliance Identified*)

The following is an illustrative combined report on compliance with applicable requirements and internal control over compliance that contains the elements in paragraphs 30 and 31. This illustrative report contains an unqualified opinion on compliance with no material weaknesses or significant deficiencies in internal control over compliance identified. The AICPA Audit Guide Government Auditing Standards *and Circular A-133 Audits* contains illustrative language for other types of reports, including reports containing qualified or adverse opinions on compliance with either material weaknesses in internal control over compliance, significant deficiencies in internal control over compliance, or both identified.

Independent Auditor's Report

[Addressee]

Compliance

We have audited Example Entity's compliance with the [*identify the applicable compliance requirements or refer to the document that describes the applicable compliance requirements*] applicable to Example Entity's [*identify the government program(s) audited or refer to a separate schedule that identifies the program(s)*] for the year ended June 30, 20X1.

Compliance with the requirements referred to above is the responsibility of Example Entity's management. Our responsibility is to express an opinion on Example Entity's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and [*insert the name of the governmental audit requirement or program-specific audit guide*]. Those standards and [*insert the name of the governmental audit requirement or program-specific audit guide*] require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the compliance requirements referred to above that could have a material effect on [*identify the*

government program(s) audited or refer to a separate schedule that identifies the program(s)] occurred.

An audit includes examining, on a test basis, evidence about Example Entity's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Example Entity's compliance with those requirements.

In our opinion, Example Entity complied, in all material respects, with the compliance requirements referred to above that are applicable to *[identify the government program(s) audited]* for the year ended June 30, 20X1.

Internal Control Over Compliance

Management of Example Entity is responsible for establishing and maintaining effective internal control over compliance with the compliance requirements referred to above. In planning and performing our audit, we considered Example Entity's internal control over compliance to determine the auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance.

Accordingly, we do not express an opinion on the effectiveness of Example Entity's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis.

A material weakness in internal control over compliance is a deficiency, or combination of deficiencies in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies, or material weaknesses in internal control over compliance.

We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of management, *[identify the body or individuals charged with governance]*, others within the entity, *[identify the legislative or regulatory body]*, and *[identify the grantor agency(ies)]* and is not intended to be and should not be used by anyone other than these specified parties.

[Signature]

[Date]

PART FOUR: COMMON METHODOLOGIES

Chapter 8: Assurance in Attestation and Direct Reporting Engagements

This chapter examines: [Introduction](#); [Assurance in Compliance Audit and Financial Audit](#); [Reasonable and Limited Assurance](#); [Attestation Engagement and Direct Reporting](#); [Levels of Assurance and Types of Audit](#); [Assertion and Audit](#); and [ISA Assurance Engagement Standard \(ISAE 3000\)](#).

8.1 Introduction

Compliance audit standards state that 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. Compliance audits may be *attestation* or *direct reporting engagements*, or both at once. This section describes the concept of assurance.

Standards state that, the intended users will wish to be confident about the reliability and relevance of the information which they use as the basis for making decisions. Audits therefore provide information based on sufficient and appropriate evidence, and auditors should perform procedures to reduce or manage the risk of reaching inappropriate conclusions.

Each audit conducted by the SAI is an assurance engagement. This assurance can either be provided through opinions and conclusions which explicitly convey the level of assurance, or it can be provided in other forms. This handbook will only describe opinions and conclusions conveying reasonable and limited assurance in accordance with the ISSAIs on compliance auditing.

Now let's examine the concept of assurance more closely:

Public officials are responsible for running public entities in compliance with the authorities governing their activities and for achieving a level of performance which is expected of them. If, for some reason, the entity fails to comply with authorities, then it means its officials will be held accountable. For example, if a government entity provides information to the Parliament about its failures to comply with authorities, or about its poor performance, this could lead to the replacement of the top officials of that entity.

Under such circumstances, a responsible party might be motivated to provide false or insufficient information to the users. Due to similar reasons, users demand an independent third-party assessment of the information. There can also be other cases, where the responsible party does not provide information to the users, and users demand an independent assessment of the actual conditions. Both cases refer to the "assurance" provided by the SAI.

Audit is defined as "a systematic process of objectively obtaining and evaluating evidence to determine whether information or actual conditions conform to established criteria". The compliance auditor will check whether the information provided by the government entities, or actual conditions in these entities comply with authorities (the relevant

laws and regulations, etc.). Following the audit, the SAI will prepare a report for the users, which includes a conclusion on the subject matter. Thus, the auditor will be providing an assurance, which reduces the risk of using the specific information. In the standards, this is

referred as “enhancing the degree of confidence of the intended users”.

An auditor performs procedures to reduce or manage the risk of providing incorrect conclusions, recognising that, owing to the inherent limitations in all audits, no audit can ever provide absolute assurance of the condition of the subject matter. This should be communicated in a transparent way. In most cases, a compliance audit will not cover all elements of the subject matter but will rely on a degree of qualitative or quantitative sampling.

8.2 Assurance in Compliance Audit and Financial Audit

It is important to differentiate the usage of “assurance” in compliance audit from its usage in financial audit. According to financial audit standards, the work conducted by an auditor is referred to as an audit only if it provides “reasonable assurance”. If the work provides “limited assurance”, it is referred to as a “review”, instead of an audit. However, compliance audit has a broader scope in methodology and covers both limited and reasonable assurance. Furthermore, limited assurance has a broader scope than a review.

8.3 Reasonable and Limited Assurance

Compliance auditing carried out by obtaining assurance can enhance the credibility of information provided by the auditor or another party. In compliance auditing there are two levels of assurance:

- **Reasonable Assurance:** conveying that, in the auditor’s opinion, the subject matter is or is not in compliance, in all material respects, with the stated criteria; and
- **Limited Assurance:** conveying that nothing has come to the auditor’s attention to cause him/her to believe that the subject matter is not compliant with the criteria.

Reasonable or limited assurance can be provided both for direct reporting and attestation engagements in compliance auditing.

The terms “reasonable” and “limited” are specifically chosen, because even if the auditor is meticulous in his work, there is always a chance that he may not identify instances of non-compliances, and therefore reach a wrong conclusion. It is not possible to provide an absolute (hundred per cent) assurance.

Levels of assurance will be examined further in planning the audit, since the decision to provide a limited or reasonable assurance will have a strong impact on the design of the audit.

8.4 Attestation Engagement and Direct Reporting

This section describes two types of audits, based on standards. Although the terms and definitions used to describe these engagements are familiar for financial auditors, they may be new for compliance auditors. It is crucial to note that concepts have been given a broader meaning related to the public sector context of compliance auditing. The concepts will be described in detail in the following sections.

Public sector audits can be categorised as two different types of audit engagements: attestation engagements and direct reporting engagements:

- 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; and

- 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, analysis or insights. The conclusion may also be expressed as a more elaborate answer to specific audit questions.

Compliance audits may be attestation or direct reporting engagements, or both at once. The difference lies in who is preparing the information; the responsible party or the auditor.

The subject matter of a compliance audit is defined by the scope of the audit. It may be activities, financial transactions or information. For attestation engagements on compliance, it is more relevant to focus on the subject matter information, which may be a statement of compliance in accordance with an established and standardised reporting framework.

The difference between the two types of audit is linked to subject matter and subject matter information and refers to the definition of audit. “Public-sector auditing can be described as a systematic process of objectively obtaining and evaluating evidence to determine whether *information* or *actual conditions* conform to established criteria”. We can broadly say that if the audit is based on evaluating information (subject matter information), it is an attestation engagement; if it is based on evaluating actual conditions (subject matter), it is a direct reporting engagement.

Let’s show this with an example which builds on the same subject matter and scope, in different environments:

Scenario 1

Responsible party:	National Tax Office (NTO) #1
Subject matter of audit:	Tax revenues of Value Added Tax (VAT)
Subject matter information:	Financial information related to VAT revenues
Criteria:	VAT law and other laws and regulations governing collection of taxes
User:	Parliament

Scenario 2:

Responsible party:	National Tax Office (NTO) #2
Subject matter of audit:	Tax revenues of Value Added Tax (VAT)
Subject matter information:	Financial information related to VAT revenues
Criteria:	VAT law and other laws and regulations governing collection of taxes
User:	Parliament

Now let's look at who creates the subject matter information, and how this influences the audit. There are two possible scenarios, which lead either to an attestation engagement, or to a direct reporting engagement.

Attestation Engagements

Standards make reference to producing subject matter information as “evaluation of subject matter against criteria”. In this situation, National Tax Office has already provided the subject matter information (evaluation) to the Parliament, in the form of a report. With their report, the officials of the responsible party are making explicit or implicit claims (assertions) that the information (evaluation) on the VAT revenue (subject matter) is true and fair in the light of the laws and regulations (criteria).

The auditor's role in this scenario is to express a conclusion (attestation) on whether the assertion made by the responsible party about the evaluation it provided is correct or not; whether the officials have indeed followed the laws and regulations as they have claimed (explicitly or implicitly). This conclusion enhances the confidence of the Parliament about the report (subject matter information) they received.

This form of audit, where the auditor gives an opinion on the subject matter information instead of on the subject matter, is called an “attestation engagement”.

Direct Reporting Engagements

In the scenario given above, no subject matter information (and therefore no assertions) has been made available by the responsible party, despite the need for this information. Therefore, the SAI decided to provide the information to the users. The audit will directly evaluate the VAT revenues (subject matter) based on criteria and provide a conclusion. Therefore, the subject matter information will be prepared by the SAI and submitted to the Parliament in the form of an audit report.

This form of audit is called “direct reporting”. In a direct reporting engagement, the audit is conducted directly on the subject matter, rather than on the subject matter information.

Scenario 1: National Tax Office (#1) presented a report to the Parliament regarding tax collection. In this scenario subject matter information has been produced by the responsible party and presented to the users in the form of a report (this information could also be in the format of a statement, statistics, etc.). When officials were producing the subject matter information, they were obliged to follow relevant legislation and other laws and regulations governing these taxes.

Scenario 2: National Tax Office (#2) does not publish reports on tax collection. Some statistics are provided in its website, but these are usually outdated and not detailed. NTO is a part of the general budget system, and due to the financial management framework, doesn't produce a separate set of financial statements. Due to the way final accounts are prepared, it isn't possible to isolate tax revenues collected by NTO from tax revenues from other sources. Recently, the Parliament has been discussing a reform initiative which aims to improve tax collection from VAT. The SAI management decided to prepare an audit report on VAT revenues and submit it to the Parliament.

Compliance Audits which are Both Attestation Engagement and Direct Reporting

Standards state that compliance audits can also be both attestation and direct reporting engagements. To explain this better, we can provide an example, which **builds on Scenario 1**.

Scenario 3: The SAI decided to prepare a report, which will assess the information provided by National Tax Office to the Parliament, regarding tax collection (Scenario 1). However, during the audit, auditors discovered that NTO’s report didn’t include information on tax exemptions. In fact, the accounting regulations didn’t require exemptions to be calculated or recorded. Therefore, it wasn’t possible to identify the actual cost of granting a VAT exemption. The SAI decided to include this issue in its report.

In this scenario, the **first part of the work is attestation engagement**, since the audit provides an assurance about the accuracy of the information provided to the Parliament. The **second part of the work is direct reporting**, since the audit is conducted directly on the subject matter. In the first part the audit is conducted on subject matter information, and in the second part it is directly on the subject matter.

8.5 Levels of Assurance and Types of Audit

To understand the wide scope of compliance audit, it is necessary to understand the link between assurance levels and types of audit. Figure 28 will help to understand how these concepts work together in practice.

Each audit conducted by the SAI will fall into one of the four cells shown in the table. However, it is important to point out that there can be overlaps, too. For example, a compliance audit can incorporate both attestation and direct reporting aspects.

Figure 26: Levels of Assurance and Types of Audit in Compliance Auditing

		Engagement type	
		Direct reporting	Attestation engagement
Assurance level	Reasonable assurance		
	Limited assurance		

Source: IDI ISSAI Handbook

8.6 Assertion and Audit

Assertion is described in the standards, as a representation, explicit or implicit, that is embodied in the activities, financial transactions and information pertaining to the audited entity, used by the auditor in considering different types of potential deviations. In the context of compliance audit, the compliance assertion would mean that the entity, including responsible public sector officials, is acting in accordance with applicable authorities (and for audits of propriety – relevant public expectations). Assertions may be embodied in subject matter information presented by the audited entity or stated explicitly in a management representation letter.

This means that when a government entity provides information about its activities, there are certain assumptions which can be made about this information. These are:

- the information provided is accurate (accuracy assertion);
- it is complete (completeness assertion); and
- most importantly, it complies with relevant laws and regulations (compliance assertion).

In fact, in many cases, these assumptions are inseparable qualities of the information provided. These qualities are referred to as assertions.

When the subject matter information is prepared by the responsible party and made available to the users, compliance audit evaluates this information by comparing it with authorities, testing the accuracy of the compliance assertion. This is attestation engagement.

As well as being assumptions, or claims made by the management, assertions also represent what the auditors are looking for in their audit. For this reason, some SAIs refer to assertions as “overall audit objectives”.

Example 1: When issuing financial statements, management of the entity makes implicit financial reporting assertions that having prepared those financial statements in accordance with the applicable financial reporting framework, such as International Public Sector Accounting Standards (IPSAS) or generally accepted government accounting standards in the particular country, the financial statements are prepared in accordance with the applicable framework, assets exist, and are owned by the entity and properly valued, etc. Similarly, management may make implicit assertions related to compliance with authorities.

Example 2: In compliance audits performed as a separate audit task or together with performance audits, the assertion could be a statement of compliance with laws or regulations, a statement of compliance with the terms of a contract, or a statement as to the effectiveness of a specific process or system. An example of an implicit assertion may be when key performance indicators are subject to audit and they are presented on the inherent assumption that there has been no undisclosed noncompliance in achieving the levels of performance as set out in the key performance indicators.

8.7 ISA Assurance Engagement Standard (ISAE 3000)

8.7.1 Introduction

This section looks at ISAE 3000; as with all such reviews, there is no substitute for reading the full document.¹⁵ The paragraph numbering are those of the standard.

This International Standard on Assurance Engagements (ISAE) deals with assurance engagements other than audits or reviews of historical financial information, which are dealt with in International Standards on Auditing (ISA) and International Standards on Review Engagements (ISRE), respectively.

2. Assurance engagements include both attestation engagements, in which a party other than the practitioner measures or evaluates the underlying subject matter against the criteria, and direct engagements, in which the practitioner measures or evaluates the underlying subject matter against the criteria. This ISAE contains requirements and application and other explanatory material specific to reasonable and limited assurance attestation engagements. This ISAE may also be applied to reasonable and limited assurance direct engagements, adapted and supplemented as necessary in the engagement circumstances.

15 <https://www.iaasb.org/publications/international-standard-assurance-engagements-isa-3000-revised-assurance-engagements-other-audits-or-0>

8.7.2 Objectives

10. In conducting an assurance engagement, the objectives of the practitioner are:

- (a) To obtain either reasonable assurance or limited assurance, as appropriate, about whether the subject matter information is free from material misstatement;
- (b) To express a conclusion regarding the outcome of the measurement or evaluation of the underlying subject matter through a written report that conveys either a reasonable assurance or a limited assurance conclusion and describes the basis for the conclusion; and
- (c) To communicate further as required by this ISAE and any other relevant ISAEs.

11. In all cases when reasonable assurance or limited assurance, as appropriate, cannot be obtained and a qualified conclusion in the practitioner's assurance report is insufficient in the circumstances for purposes of reporting to the intended users, this ISAE requires that the practitioner disclaim a conclusion or withdraw (or resign) from the engagement, where withdrawal is possible under applicable law or regulation.

8.7.3 Requirements: Conduct of an Assurance Engagement in Accordance with ISAEs

Complying with Standards that are Relevant to the Engagement

14. The practitioner shall comply with this ISAE and any subject matter specific ISAEs relevant to the engagement.

15. The practitioner shall not represent compliance with this or any other ISAE unless the practitioner has complied with the requirements of this ISAE and any other ISAE relevant to the engagement.

Text of an ISAE

16. The practitioner shall have an understanding of the entire text of an ISAE, including its application and other explanatory material, to understand its objectives and to apply its requirements properly.

Complying with Relevant Requirements

17. Subject to the following paragraph, the practitioner shall comply with each requirement of this ISAE and of any relevant subject matter specific ISAE unless, in the circumstances of the engagement the requirement is not relevant because it is conditional and the condition does not exist. Requirements that apply to only limited assurance or reasonable assurance engagements have been presented in a columnar format with the letter "L" (limited assurance) or "R" (reasonable assurance) after the paragraph number.

18. In exceptional circumstances, the practitioner may judge it necessary to depart from a relevant requirement in an ISAE. In such circumstances, the practitioner shall perform alternative procedures to achieve the aim of that requirement. The need for the practitioner to depart from a relevant requirement is expected to arise only where the requirement is for a specific procedure to be performed and, in the specific circumstances of the engagement, that procedure would be ineffective in achieving the aim of the requirement.

Failure to Achieve an Objective

19. If an objective in this ISAE or a relevant subject matter specific ISAE cannot be achieved, the practitioner shall evaluate whether this requires the practitioner to modify the

practitioner's conclusion or withdraw from the engagement (where withdrawal is possible under applicable law or regulation). Failure to achieve an objective in a relevant ISAE represents a significant matter requiring documentation in accordance with paragraph 79 of this ISAE.

8.7.4 Ethical Requirements

20. The practitioner shall comply with Parts A and B of the IESBA Code related to assurance engagements, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding.

8.7.5 Acceptance and Continuance

21. The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and assurance engagements have been followed by the firm and shall determine that conclusions reached in this regard are appropriate.

8.7.6 Professional Scepticism, Professional Judgment, and Assurance Skills and Techniques

37. The practitioner shall plan and perform an engagement with professional scepticism, recognizing that circumstances may exist that cause the subject matter information to be materiality misstated.

38. The practitioner shall exercise professional judgment in planning and performing an assurance engagement, including determining the nature, timing and extent of procedures.

39. The practitioner shall apply assurance skills and techniques as part of an iterative, systematic engagement process.

8.7.7 Planning and Performing the Engagement

Planning

40. The practitioner shall plan the engagement so that it will be performed in an effective manner, including setting the scope, timing and direction of the engagement, and determining the nature, timing and extent of planned procedures that are required to be carried out in order to achieve the objective of the practitioner.

Materiality

44. The practitioner shall consider materiality

Understanding the Underlying Subject Matter and Other Engagement Circumstances (p45)

8.7.8 Obtaining Evidence

Risk Consideration and Responses to Risks (paragraph #50)

Work Performed by a Practitioner's Expert (paragraph #52)

Written Representations

56. The practitioner shall request from the appropriate party(ies) a written representation.

Requested Written Representations Not Provided or Not Reliable (paragraph #60)

8.7.9 Subsequent Events

61. When relevant to the engagement, the practitioner shall consider the effect on the subject matter information and on the assurance report of events up to the date of the assurance report, and shall respond appropriately to facts that become known to the practitioner after the date of the assurance report, that, had they been known to the practitioner at that date, may have caused the practitioner to amend the assurance report. The extent of consideration of subsequent events depends on the potential for such events to affect the subject matter information and to affect the appropriateness of the practitioner's conclusion. However, the practitioner has no responsibility to perform any procedures regarding the subject matter information after the date of the assurance report.

8.7.10 Other Information

62. When documents containing the subject matter information and the assurance report thereon include other information, the practitioner shall read that other information to identify material inconsistencies, if any, with the subject matter information or the assurance report and, if on reading that other information, the practitioner:

- (a) Identifies a material inconsistency between that other information and the subject matter information or the assurance report; or
- (b) Becomes aware of a material misstatement of fact in that other information that is unrelated to matters appearing in the subject matter information or the assurance report, the practitioner shall discuss the matter with the appropriate party(ies) and take further action as appropriate.

8.7.11 Description of Applicable Criteria

63. The practitioner shall evaluate whether the subject matter information adequately refers to or describes the applicable criteria.

8.7.12 Forming the Assurance Conclusion

64. The practitioner shall evaluate the sufficiency and appropriateness of the evidence obtained in the context of the engagement and, if necessary, in the circumstances, attempt to obtain further evidence. The practitioner shall consider all relevant evidence, regardless of whether it appears to corroborate or to contradict the measurement or evaluation of the underlying subject matter against the applicable criteria.

8.7.13 Preparing the Assurance Report

67. The assurance report shall be in writing and shall contain a clear expression of the practitioner's conclusion about the subject matter information.

68. The practitioner's conclusion shall be clearly separated from information or explanations that are not intended to affect the practitioner's conclusion, including any Emphasis of Matter, Other Matter, findings related to particular aspects of the engagements, recommendations or additional information included in the assurance report. The wording used shall make it clear that an Emphasis of Matter, Other Matter, findings, recommendations or additional information is not intended to detract from the practitioner's conclusion.

Assurance Report Content

69. The assurance report shall include at a minimum the following basic elements:

- (a) A title that clearly indicates the report is an independent assurance report;
- (b) An addressee;
- (c) An identification or description of the level of assurance obtained by the practitioner, the subject matter information and, when appropriate, the underlying subject matter. When the practitioner's conclusion is phrased in terms of a statement made by the appropriate party, that statement shall accompany the assurance report, be reproduced in the assurance report or be referenced therein to a source that is available to the intended users;
- (d) Identification of the applicable criteria;
- (e) Where appropriate, a description of any significant inherent limitations associated with the measurement or evaluation of the underlying subject matter against the applicable criteria;
- (f) When the applicable criteria are designed for a specific purpose, a statement alerting readers to this fact and that, as a result, the subject matter information may not be suitable for another purpose;
- (g) A statement to identify the responsible party and the measurer or evaluator if different, and to describe their responsibilities and the practitioner's responsibilities;
- (h) A statement that the engagement was performed in accordance with this ISAE or, where there is a subject-matter specific ISAE, that ISAE;
- (i) A statement that the firm of which the practitioner is a member applies ISQC 1, or other professional requirements, or requirements in law or regulation, that are at least as demanding as ISQC 1. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements in law or regulation, applied that are at least as demanding as ISQC 1;
- (j) A statement that the practitioner complies with the independence and other ethical requirements of the IESBA Code, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements. If the practitioner is not a professional accountant, the statement shall identify the professional requirements, or requirements imposed by law or regulation, applied that are at least as demanding as Parts A and B of the IESBA Code related to assurance engagements;
- (k) An informative summary of the work performed as the basis for the practitioner's conclusion. In the case of a limited assurance engagement, an appreciation of the nature, timing, and extent of procedures performed is essential to understanding the practitioner's conclusion. In a limited assurance engagement, the summary of the work performed shall state that:
 - (i) The procedures performed in a limited assurance engagement vary in nature and timing from, and are less in extent than for, a reasonable assurance engagement; and

(ii) Consequently, the level of assurance obtained in a limited assurance engagement is substantially lower than the assurance that would have been obtained had a reasonable assurance engagement been performed.

(l) The practitioner's conclusion:

(i) When appropriate, the conclusion shall inform the intended users of the context in which the practitioner's conclusion is to be read;

(ii) In a reasonable assurance engagement, the conclusion shall be expressed in a positive form;

(iii) In a limited assurance engagement, the conclusion shall be expressed in a form that conveys whether, based on the procedures performed and evidence obtained, a matter(s) has come to the practitioner's attention to cause the practitioner to believe that the subject matter information is materially misstated;

(iv) The conclusion in (ii) or (iii) shall be phrased using appropriate words for the underlying subject matter and applicable criteria given the engagement circumstances and shall be phrased in terms of:

- a. The underlying subject matter and the applicable criteria;
- b. The subject matter information and the applicable criteria; or
- c. A statement made by the appropriate party.

(v) When the practitioner expresses a modified conclusion, the assurance report shall contain:

- a. A section that provides a description of the matter(s) giving rise to the modification; and
- b. A section that contains the practitioner's modified conclusion.

(m) The practitioner's signature;

(n) The date of the assurance report. The assurance report shall be dated no earlier than the date on which the practitioner has obtained the evidence on which the practitioner's conclusion is based, including evidence that those with the recognised authority have asserted that they have taken responsibility for the subject matter information; and

(o) The location in the jurisdiction where the practitioner practices.

72. The practitioner shall express an unmodified conclusion when the practitioner concludes:

(a) In the case of a reasonable assurance engagement, that the subject matter information is prepared, in all material respects, in accordance with the applicable criteria; or

(b) In the case of a limited assurance engagement, that, based on the procedures performed and evidence obtained, no matter(s) has come to the attention of the practitioner that causes the practitioner to believe that the subject matter information is not prepared, in all material respects, in accordance with the applicable criteria.

74. The practitioner shall express a modified conclusion in the following circumstances:

- (a) When, in the practitioner's professional judgment, a scope limitation exists and the effect of the matter could be material (see paragraph 66). In such cases, the practitioner shall express a qualified conclusion or a disclaimer of conclusion; or
- (b) When, in the practitioner's professional judgment, the subject matter information is materially misstated. In such cases, the practitioner.

8.7.14 Documentation

79. The practitioner shall prepare on a timely basis engagement documentation that provides a record of the basis for the assurance report that is sufficient and appropriate to enable an experienced practitioner, having no previous connection with the engagement, to understand:

- (a) The nature, timing and extent of the procedures performed to comply with relevant ISAEs and applicable legal and regulatory requirements;
- (b) The results of the procedures performed, and the evidence obtained; and
- (c) Significant matters arising during the engagement, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

Chapter 9: Documentation, Working Papers and Communication

This chapter examines: [Introduction](#); [Documentation](#); [Working Papers](#); and [Communications](#).

9.1 Introduction

The basic principles of Documentation, Working Papers and Communication are common to all forms of Compliance Auditing and are, thus, examined together in detail in this chapter. This work builds on the material outlined in the relevant standards and is not intended to contradict this. If there are any conflicts, then the standards prevail.

The credibility and impact of audit depend on the quality work that SAs do. Proper documentation throughout an audit cycle (from planning to report stages) helps SAs in producing high quality audit reports. Continuous good communication with the audited entity is also important during the entire audit process. The chapter explains how auditors can make use of documentation and communication in a compliance audit to improve the quality of their work. Since limited guidance is available in the ISSAI regarding these two concepts inasmuch as they relate to compliance audit, good practices have been adapted to provide useful guidance.

The IDI ISSAI Implementation Handbooks provide excellent material for this chapter and have been relied upon extensively.

9.2 Documentation

9.2.1 Overview

Audit documentation is the written record of the basis on which auditors draw their conclusions or opinion in a compliance audit. Thus, documents prepared during planning, conducting or reporting stage of a compliance audit can be examined to see whether or not auditors have carried out a compliance audit as per the ISSAI.

Documents will contain sufficient information to enable an experienced auditor, having no previous connection with the audit:

- The relationship between the subject matter, criteria, audit scope;
- Risk assessment, audit strategy;
- Audit plan and the nature, timing, extent and results of the procedures performed;
- Evidence obtained in support of the auditors conclusion or opinion;
- The reasoning behind all significant matters that required the exercise of professional judgment; and
- Conclusions.

Proper documentation helps reviewers of audit work to understand what has been done, how it has been done, and why it has been done. Auditors need to do proper documentation at every stage of the audit process. For any compliance audit, documents should indicate:

- How the auditors decided the subject matter, criteria and scope;
- What analytical and other audit procedures were carried out to collect audit evidence to determine whether the subject matter was/was not in compliance with the criteria and

- That the conclusion and opinion in the report were based on sufficient and appropriate evidence.

Audit documentation should be prepared in sufficient detail to provide a clear understanding of its purpose, source, and the conclusions reached. Also, the documentation should be appropriately organised to provide a clear link to the significant findings or issues. Office memoranda, confirmations, correspondence, schedules, audit programs, and letters of representation are some examples of documents. Audit documentation may be in the form of paper, electronic files, or other media.

9.2.2 What to Document

The auditor should document:

- a. The risk assessment procedures performed, including those related to gaining an understanding of internal control system;
- b. His or her responses to the assessed risks of material noncompliance, the procedures performed to test compliance with the applicable compliance requirements, and the results of those procedures, including any tests of controls;
- c. Materiality (qualitative and quantitative);
- d. The basis on which they were determined; and
- e. How the audit team complied with the specific public sector audit requirements (if any) that are supplementary to auditing standards.

The auditor's documentation of evidence regarding identified or suspected non-compliance with authorities may include, for example:

- a. Copies of records or documents; and
- b. Minutes of discussions held with management, those charged with governance, or other parties inside or outside the entity.

Auditors are required to document the audit procedures performed, evidence obtained, and conclusions reached with respect to compliance audit criteria used in audit. Auditors would develop/maintain documents that will clearly show that the work was in fact performed.

In determining the nature and extent of the documentation for a typical compliance audit , auditors may be advised to consider the following factors:

- Nature of the auditing procedures performed;
- Risk of material non-compliance with the applicable criteria, and auditors' response to the assessed risks;
- Extent to which professional judgment was applied in work especially in the context of materiality consideration; and
- Materiality of the evidence obtained against criteria.

Documentation should be sufficiently detailed to enable an experienced auditor, with no prior knowledge of the audit, to understand the following: the relationship between the subject matter, the criteria, the audit scope, the risk assessment, the audit strategy and audit plan and the nature, timing, extent and results of the procedures performed; the evidence obtained in support of the auditor's conclusion or opinion; the reasoning behind all significant matters that required the exercise of professional judgment; and the related conclusions.

9.2.3 When to Document

Documentation should be prepared at the appropriate time and should provide a clear understanding of the criteria used, the scope of the audit, the judgments made, the evidence obtained and the conclusions reached.

Documentation should take place throughout the entire audit process. Different supporting documentation will be gathered at various phases during the audit process to support outputs at each stage of the audit.

Timeliness of documentation is also important. Preparing sufficient and appropriate audit documentation on a timely basis helps to enhance the quality of the audit and facilitates the effective review and evaluation of the audit evidence obtained and conclusions reached before the auditors' report is finalised. Documentation prepared after the audit work has been performed is likely to be less accurate than documentation prepared at the time such work is performed. All working papers should be assembled and reviewed prior to issuance of the audit report.

The auditor should prepare relevant audit documentation before the audit report is issued, and the documentation should be retained for an appropriate period of time.

9.2.4 Document Retention

SAI should have policies and procedures consistent with their laws and auditing standards to maintain documentation of their work. Documentation retention policies ensure that relevant record is available for use for a certain number of years after an audit. These policies and procedures usually describe:

- (a) documents covered in their scope;
- (b) form in which the documents would be kept/archived;
- (c) period for which the documents would be retained; and
- (d) how these documents can be accessed when needed.

These requirements may be due to the historical significance of certain types of documents which, for example, may require indefinite retention in the country's national archives. There may also be additional requirements related to national security classifications, including how documentation is stored. Public sector auditors familiarise themselves with applicable legislation in regard to retention of documentation.

9.2.5 Confidentiality and Transparency Issues

SAI need to establish and ensure that auditors comply with ethical requirements to observe at all times the confidentiality of information contained in audit documentation, unless specific authority has been given by the entity to disclose such information, or there is a legal or professional duty to do so. There is an ongoing need in the public sector to balance confidentiality with the need for transparency and accountability.

The balance between confidentiality and transparency requires professional judgment to ensure that documentation of a confidential nature is clearly identified and treated as such, while at the same time granting access as appropriate. It is therefore important to be familiar with the SAIs' policies and procedures addressing confidentiality.

Such procedures might include types of audit documentation to be considered confidential, types of audit documentation to be made available to the public, clearly defined lines of

responsibility for authorizing disclosure of audit documentation and routines for making such information available if required.

Furthermore, public sector auditors may have additional statutory responsibilities related to confidentiality. These responsibilities may be based on the mandate of SAI or legislation related to official secrets or privacy. Such legislation, for example, could relate to audits of defence, health, social service or tax agencies. Public sector auditors familiarise themselves with the particular local requirements related to confidentiality to which they are bound.

9.2.6 Legislation

Public sector auditors also familiarise themselves with any legislation that grants public access to audit correspondence, for example where electronic or other post journals are open to public scrutiny. This type of correspondence may include letters to and from the audited entity, or other parties, related to the gathering of audit evidence, as well as considerations and judgments related to audit issues. It is not unusual in the public sector to have to respond to requests from outside parties to obtain access to audit documentation. This can be especially sensitive when the outside party attempts to obtain information indirectly from the audit organisation that it is unable to obtain directly from the audited entity.

As a matter of principle, when the audited entity has a statutory obligation to gather and retain certain information, requests from outside parties for such information are normally referred to the audited entity. In situations where public sector auditors consider granting access to audit documentation, they normally consult with relevant parties (such as the audited entity to whom the request relates) prior to the information being disclosed.

In some environments, public sector audit work is contracted out by the SAI to other auditors. The acceptance of such appointments normally requires the auditor performing the work to acknowledge that audit documentation may be subject to inspection by the Supreme Audit Institution that appointed the auditor. The audit documentation may also be subject to inspection by review agencies that have statutory rights of access to information relevant to the auditor's duties.

9.3 Working Papers

9.3.1 Components of Working Papers

Based on the standards and best practices, following are some common components of working papers that most audit documentation follows:

- The working paper has:
 - Name of audit;
 - Title;
 - Auditor's initials;
 - Date completed;
 - Page number and reference;
 - Source, purpose, procedures, results, conclusions; and
 - Two-way cross-references.
- The working paper is:
 - Neat and legible;
 - Referenced to the programme; and

- Understandable without further explanation
- Important calculations are verified;
- Source documents are included as necessary;
- If a document was produced by the entity, it is written on the working paper; and
- A review has been indicated and all points were cleared.

9.3.2 Organising Working Papers

According to ISSAI, documentation needs to be organised in a way that provides a clear and direct link between the findings and the evidence that supports them. Working papers can be organised in many different ways. It is the auditor who determines how to do it, sometimes with the system or practices that exist in the SAI. The auditor may have many working papers supporting the audit, but to be understandable to an outside party, they need to be explained and organised. Using a summary memo facilitates this process.

The summary memo can be called a lead sheet, a conclusions form, or a top memo based on the SAI practice and norms. It might have components that differ from those described here, also based on the SAI's practice.

Summary memoranda will make the supervisor's or reviewer's work easier. Writing these memos forces the auditor to clarify his or her thoughts and document them in writing before completing the audit, which makes it easier to understand the working papers.

A summary memorandum summarises a group of working papers. In the hierarchy of working papers, a summary memo usually comes third, even though it may be written last. The hierarchy is as follows:

- Audit Objective;
- Audit programme;
- Summary memorandum; and
- Detailed Working Papers.

Table 10: Example of a Summary Memorandum (1)

In an audit of a purchasing department, after gathering information and doing a risk assessment the auditor decides that the overarching objective is to determine if the purchasing department complies with significant purchasing policies. Under that overarching objective are three sub-objectives—to determine the following:

- Are purchases of equipment exceeding \$9000 conducted in accordance with policy?
- Are purchasing procedures written in accordance with policy?
- Are professional contracts in accordance with policy?

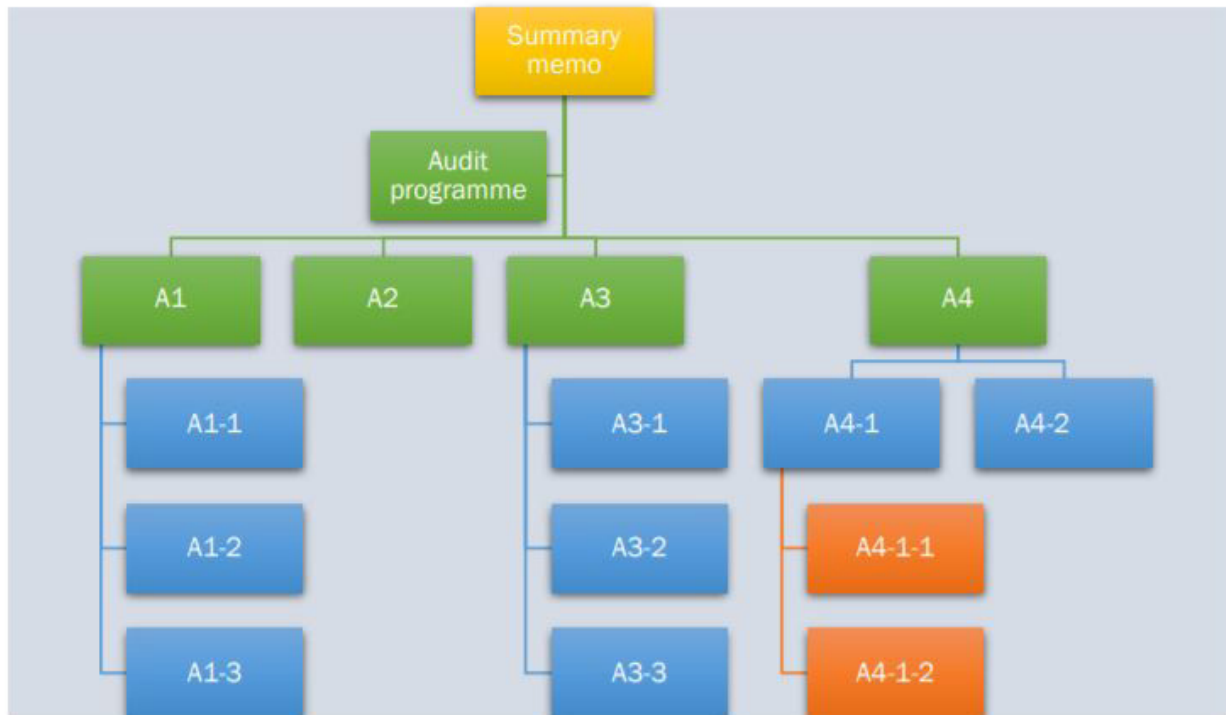
The auditor will create a set of working papers to support each sub-objective, and will use letters to designate groups of working papers:

1. Working paper set A answers sub-objective 1: whether purchases of equipment exceeding \$9000 were conducted in accordance with policy.
2. Working paper set B answers sub-objective 2: whether purchasing procedures are written in accordance with policy.
3. Working paper set C answers sub-objective 3: whether professional contracts are in accordance with policy.

The summary memo for sub-objective 1 summarises what working paper series A accomplished and how the auditor answered the audit objective, with all the related evidence. Then A-1, A-2, A-3, etc. speak to the performance and results of each audit procedure.

The summary memo is a kind of narrative version of the audit programme and in the hierarchy might fall above or beneath the programme. The working paper hierarchy might look like this:

Figure 27: Working Paper Hierarchy



There can be a “meta” or master summary memorandum that summarises working paper series A, B, and C and speaks to the overarching audit objective: “Does the purchasing department comply with significant policies?” The auditor can prepare summary memoranda for each audit procedure. The working paper series A-4 above contains plenty of working papers and may warrant a summary to help the reviewer sort through the group and discern what the auditor did.

What is included in a summary memo? The summary memo includes the components of the working paper – source, purpose, procedure, results and conclusion, with a narrative description of these five components in every working paper. Below is an example of a summary memo for series A.

Table 11: Example of a Summary Memorandum (2)

Source
Interviews, observations, and testing described in working paper series A.
Purpose
To answer the sub-objective “Are purchases of equipment exceeding \$9000 conducted in accordance with state law?”
Procedure
We satisfied programme steps in the area decided, which called on us to: <ul style="list-style-type: none"> • Reiterate programme step 1; • Reiterate programme step 2; and • Reiterate programme step 3.
Results
We noted several significant items of non-compliance: <ul style="list-style-type: none"> • Summarise results of programme step 1; • Summarise results of programme step 2; and • Summarise results of programme step 3.
Conclusion
The purchasing department did not comply with significant purchasing policies regarding purchases of equipment exceeding O\$9,000. In particular, the department allowed the same person to initiate, approve, and receive equipment purchases over O\$9,000. This issue has been developed into a finding for the report. We did not find any questionable purchases.

The summary memo can serve as an initial draft of the report. Instead of referring to a finding in a working paper outside of the summary memo, the auditor can include it in the summary memo, or can formalise the section where the auditor discusses the objective and conclusion and later add it to the report.

The summary memo can be very detailed or highly summarised. A summary memo can be a restatement of each supporting working paper under it, plus an overarching conclusion that sums up the whole set. Or it can be an overarching conclusion that sums up the whole set. A good way to determine how much detail the summary memo should contain is to refer to the practices set at the SAI.

Summary memos can take care of a good number of the required contents of working papers. The standard requires that the auditor document the following in the working papers:

- Objective, scope, and methodology;
- Nature, timing, and extent of procedures ;
- Audit evidence obtained and its source and the conclusions reached;
- Support for significant judgments, findings, conclusions, and recommendations; and
- Evidence of supervisory review.

The standards are not explicit about maintaining a summary memo. But it is good to have this for the sake of the auditors’ and the reviewers’ jobs. Auditors could use a summary memo to do the majority of this work. Auditors could take care of only part of these requirements in the detailed, supporting working papers.

9.3.3 How to Review the Working Papers

It is often very difficult by looking at a set of working papers to understand what the auditor was thinking and to retrace the thought process during an audit. It may take hours to get a sense of the overall purpose of the working papers. Two simple guiding principles of working paper review make the task an easy process:

- Check concepts before procedures; and
- Review working papers beginning at the top of the working paper hierarchy.

Table 12: Check Concepts Before Procedures

An audit team expressed an opinion on a university's bond issues. One of the more senior auditors took the lead in auditing bond arbitrage, a technical subject. He spent two days auditing and creating a good-looking working paper. It was a huge, foldout spreadsheet that had several columns and rows and had plenty of coloured tick marks and numbers.

The supervisor started her review of this spreadsheet. She re-footed and re-cross-footed the columns. She checked the meaning of all the tick marks and added one of her own. And then, after about half a day of reviewing it, she realised that the concept behind the working paper was flawed. The senior auditor had gone down a trail and tested attributes that did not pertain to the audit objective.

The whole working paper was scrapped. So, time spent by the auditor—two days, and the supervisor—half-a-day, was not necessary. Had the supervisor checked the concept of the working paper before the procedure, she could have saved her time and audit resources.

Following the hierarchy of working papers is important to consider. Only if the top of the hierarchy works well and is understandable should the reviewer delve into the working papers at the bottom of the hierarchy. This saves time and effort.

As we have seen, the hierarchy of working papers is as follows:

- Audit Objective;
- Audit Programme;
- Summary Memorandum; and
- Detailed Working Papers

The first thing the reviewer should look at is the audit objective. If the audit objective is flawed, s/he can stop right there. S/he can give the working papers back to the auditor and tell him or her to work on the objective and change the working papers accordingly.

Once satisfied with the audit objective, the reviewer can review either the summary memo or the audit programme. Because some auditors do not create summary memos, s/he may have to look at the programme. Or s/he may have to look at the audit programme if the summary memo is not useful.

If a reviewer sees that the programme is disjointed and does not help satisfy the audit objective, s/he can again stop the review of the working papers and return them to the auditor. There is no reason to proceed further until the programme is rewritten.

Assuming that the auditor's audit programme and summary memo are good, the reviewer can move on to the detailed supporting working papers. Those working papers should satisfy steps of the audit programme.

9.4 Communications

9.4.1 The Role of Communication

Communication takes place at all audit stages; before the audit starts, during initial planning, during the audit proper, and at the reporting phase. Any significant difficulties encountered during the audit, as well as instances of material non-compliance should be communicated to the appropriate level of management or those charged with governance. The auditor should also inform the responsible party of the audit criteria.

Good communication with the audited entity throughout the audit process may help make the process more effective and constructive. Effective two-way communication is important in assisting:

- a. The auditor and those charged with governance in understanding matters related to the audit in context, and in developing a constructive working relationship. This relationship is developed while maintaining the auditor's independence and objectivity;
- b. Public sector auditors need to be particularly sensitive to meet the needs and expectations of the legislature or appropriate regulators about matters communicated to other governance levels, particularly where the matters may be of broad public interest or speculation; and
- c. The auditor in obtaining from those charged with governance information relevant to the audit. For example, those charged with governance may assist the auditor in understanding the entity and its environment, in identifying appropriate sources of audit evidence, and in providing information about specific transactions or events.

9.4.2 The Communication Process

SAI need to have a system in place to see that requires the auditor to evaluate whether the two-way communication between the auditor and those charged with governance has been adequate for the purpose of the audit. If the two-way communication is not adequate, it is advised that the auditor take appropriate action. In the public sector, appropriate action may include communicating with the legislature or the appropriate regulators, or funding agencies.

Law or regulation may restrict the auditor's communication of certain matters with those charged with governance. For example, laws or regulations may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act. In some circumstances, potential conflicts between the auditor's obligations of confidentiality and obligations to communicate may be complex. In such cases, the auditor may consider obtaining legal advice.

Communication takes place at various phases and at various levels.

9.4.3 Communication at the Planning Phase

Auditors interact with the appropriate level of management and those charged with governance considering relevant provisions of laws that govern such interaction. Key points that may be reviewed with the audited entity include:

- Overall audit strategy;

- Timing and duration of the audit;
- Responsibilities of auditors and the audited entity. Usually, a focal person is notified by the audited entity who is available to provide necessary information and support throughout audit; and
- Audit criteria. In cases where such criteria are not straight forward, auditors need to review and agree on criteria in consultation with management.

9.4.4 Communication at the Gathering Evidence Phase

While gathering evidence for their findings, auditors' interaction with the audited entity becomes extremely critical. As stressed above, the quality of audit depends on the sufficiency and appropriateness of audit evidence. Auditors maintaining good communication with the audited entity are better placed to review initial findings with the relevant officials in the audited entity, firm up their findings, and gather sufficient appropriate evidence in support.

For the audited entity as well, continuous interaction helps in identifying weak areas and taking steps toward rectification. Any significant difficulties encountered during the audit, as well as instances of material non-compliance are promptly communicated to the appropriate level of management, or to those charged with governance. Though different SAI may have different approaches for communication with the audited entity, it may be desirable to communicate all identified instances of non-compliance to management so that the management can take appropriate actions.

9.4.5 Communication at the Reporting and Follow-Up Phase

Auditors are required to prepare a written report for the intended users. The practice of finalising report may differ from SAI to SAI but some SAI obtain and incorporate the views of management in the report. This allows the intended users to look at management's viewpoint while reviewing auditors' report.

Some SAI can, according to their audit mandate, order the audited entity to correct identified instances of non-compliance. In doing so, public sector auditors determine whether their independence and objectivity will be impaired and take appropriate action to avoid such impairment.

Chapter 10: Gathering and Evaluating Evidence and Forming Conclusions

This chapter examines: [Overview](#); [Quantity and Quality of Available Evidence](#); [Sufficiency, Appropriateness and Reliability of Audit Evidence](#); [Gathering of Evidence](#); [Evidence Gathering Techniques](#); [Evaluating Evidence](#); and [Forming Conclusions](#).

10.1 Overview

As with the previous chapter, the IDI ISSAI Implementation Handbooks provide excellent material for this chapter and have been relied upon extensively.

Audit evidence is the information used by the auditor in arriving at the conclusions on which the auditor's conclusion or opinion is based. Auditors design and apply appropriate audit procedures to obtain sufficient and appropriate audit evidence in order to form a conclusion or opinion as to whether a subject matter complies, in all material respects, with established criteria. To cover the audit scope, the auditor has to decide when the audit evidence is sufficient and appropriate to give provision for the basis of conclusion or opinion.

In the planning phase, auditors review the:

- a. internal controls established by the audited entity to prevent, detect, and rectify instances of non-compliance, and
- b. whether there is an organisational unit within the audited entity for management of controls and other risks.

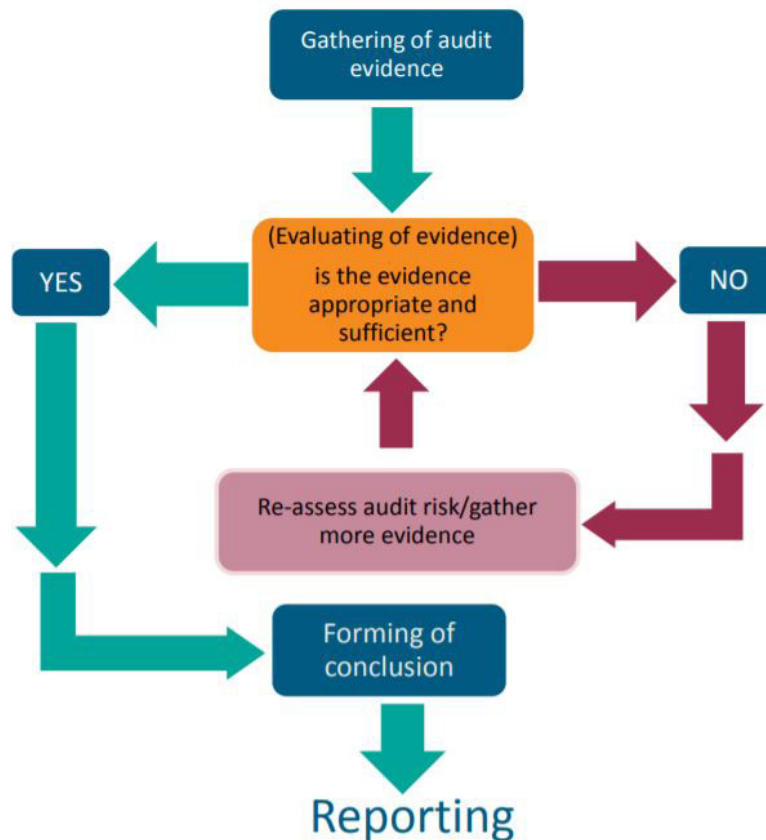
Based on this review auditors identify control risks and other risks and keep these in consideration while they start gathering audit evidence.

The procedures depend on the particular subject matter and criteria and auditors' professional judgment.

When the risks of noncompliance are significant and auditors plan to rely on the controls in place, such controls are required to be tested. When controls are not considered reliable, auditors plan and perform substantive procedures to respond to the identified risks. Auditors perform additional substantive procedures when there are significant risks of non-compliance. If the audit approach consists only of substantive procedures, analytical tests and tests of details are performed.

The compliance auditor will often need to combine and compare evidence from different sources in order to meet the requirements for sufficiency and appropriateness of audit evidence. Professional judgment needs to be exercised in considering the quantity and quality of available evidence when performing the engagement, in particular when determining the nature, timing and extent of procedures.

Figure 28: Iterative Process of Evidence Gathering and Re-assessment of Risk



10.2 Quantity and Quality of Available Evidence

Audit evidence would be considered sufficient (quantitative) when it can persuade a knowledgeable person that the findings are reasonable. Audit evidence would be considered appropriate when it is relevant, directly linked to the criteria and subject matter and reliable.

The quantity or quality of available evidence is affected by:

- a. The characteristics of the subject matter and subject matter information. For example, less objective evidence might be expected when the subject matter information is future oriented rather than historical; and
- b. In circumstances when evidence that could reasonably be expected to exist is not available because of, for example, the timing of the auditor's engagement, an entity's document retention policy, inadequate information systems, or a restriction imposed by the responsible party.

10.3 Sufficiency, Appropriateness and Reliability of Audit Evidence

The sufficiency and appropriateness of evidence are interrelated. Sufficiency is the measure of the quantity of evidence. The quantity of evidence needed is affected by the risks of the subject matter information being non-compliant or prone to compliance deviation (i.e. the higher the risks, the more evidence is likely to be required) and also by the quality of such evidence (i.e. the higher the quality, the less may be required). Obtaining more evidence, however, may not compensate for its poor quality.

Appropriateness is the measure of the quality of evidence; that is, its relevance and its reliability in providing support for the auditor's conclusion.

The auditor's professional judgment as to what constitutes sufficient appropriate evidence is influenced by factors as following:

- Significance of a potential non-compliance or compliance deviation and the likelihood of its having a material effect, individually or when aggregated with other potential non-compliance, on the subject matter information;
- Effectiveness of the responsible party's responses to address the known risk of non-compliance or compliance deviation;
- Experience gained during previous audit with respect to similar potential non-compliance or compliance deviation;
- Results of procedures performed, including whether such procedures identified specific non-compliance or compliance deviation;
- Source and reliability of the available information;
- Persuasiveness of the evidence; and
- Understanding of the responsible party and its environment.

The reliability of evidence is influenced by its source and by its nature and is dependent on the individual circumstances under which it is obtained. Generalisations about the reliability of various kinds of evidence can be made; however, such generalisations are subject to important exceptions. Even when evidence is obtained from external sources, circumstances may exist that could affect its reliability.

For example, evidence obtained from an external source may not be reliable if the source is not knowledgeable or objective. While recognizing that exceptions may exist, the following generalisations about the reliability of evidence may be useful, evidence is likely to be more reliable when:

- It is obtained from sources outside the responsible party;
- It is generated internally, when the related controls are effective;
- Obtained directly by the auditor. For example, observation of the application of a control is more reliable than evidence obtained indirectly or by inference, for example, inquiry about the application of a control; and
- It exists in documentary form, whether paper, electronic, or other media. For example, the minutes of a meeting which is recorded concurrently during the meeting is generally more reliable than a subsequent oral representation of what was discussed.

More assurance is ordinarily obtained from consistent evidence obtained from different sources, or of a different nature, than from items of evidence considered individually. In addition, obtaining evidence from different sources or of a different nature may either corroborate other evidence or indicate that an individual item of evidence is not reliable. In cases, where evidence obtained from one source is inconsistent with that obtained from another, auditor needs to determine what additional procedures are needed to resolve the inconsistency.

In terms of obtaining sufficient appropriate evidence, it is generally more difficult to obtain assurance about subject matter information **covering a period** than about subject matter information **at a point in time**. In addition, conclusions provided on processes ordinarily are limited to the period covered by the engagement; auditor provides no conclusion about whether the process will continue to function in the specified manner in the future.

The scope of the audit determines where to gather audit evidence, meaning that the audit evidence can be collected from within or outside the entity, or be produced directly by the auditor. The auditor should consider using different sources in the evidence gathering process. The audit evidence may be physical, documentary, oral or analytical depending on the audit scope.

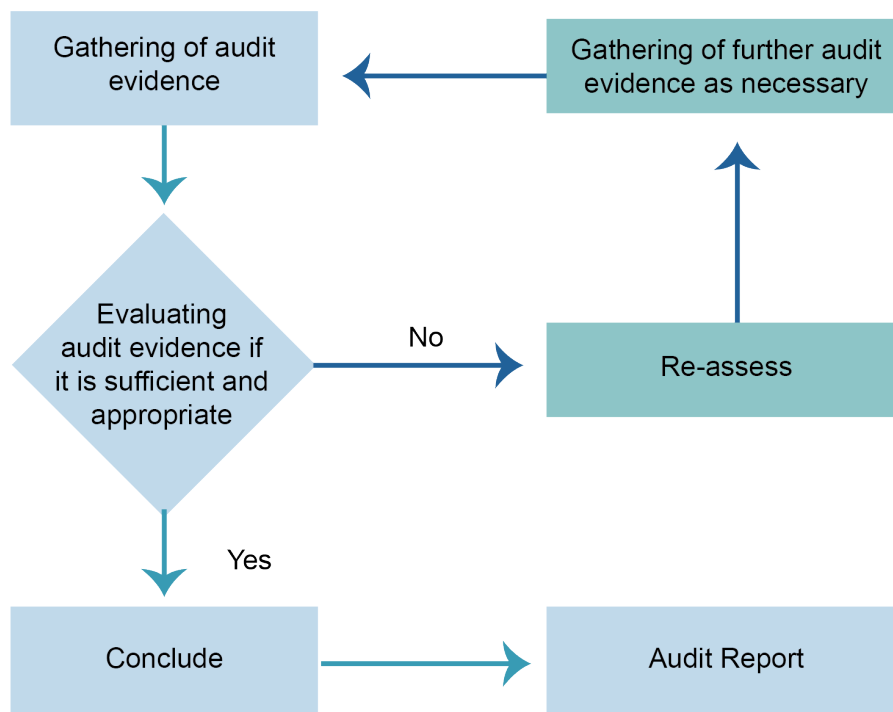
10.4 Gathering of Evidence

Gathering of sufficient and appropriate audit evidence is a systemic and iterative process as it involves:

- Gathering evidence by performing appropriate audit procedures;
- Evaluating the evidence obtained as to its sufficiency (quantity) and appropriateness (quality); and
- Re-assessing risk and gathering further evidence as necessary.

As the auditor performs planned audit procedures, the audit evidence obtained may lead the auditor to modify the nature, timing or extent of other planned audit procedures. Information may come to the auditor's attention that differs significantly from the information on which the risk assessments were based at the outset. For example, the extent of deviation that the auditor detects by performing audit procedures may alter the auditor's judgment about the risk assessments and may indicate a material weakness in internal control. In such circumstances the auditor should re-evaluate the planned audit procedures based on revised considerations of assessed risks.

Figure 29: Evidence Decision Making Process



10.5 Evidence Gathering Techniques

These are discussed in paragraph 4.4.5 above and are summarised for a VAT audit, in Table 13.

Table 13: Summary of Evidence Gathering Techniques

Technique	Application for VAT Audit
Observation	Auditors observe whether (a) a Risk Management Unit (RMU) is established and (b) it is staffed with competent staff. Auditors may visit the RMU in the National Tax Office (NTO) and see how the staff is working.
Inspection	Auditors can randomly select a few VAT cases and examine whether the tax has been correctly calculated. Further, auditors may also do the same exercise for VAT refunds which is high risk area.
Inquiry	Auditors inquire from the government officials involved in VAT management through written letters, discussion, interviews, or surveys about applicable slabs, exemptions, and other procedural requirements to see whether or not the officers are on the same page. In many cases, non-compliance occurs because the government officials concerned do not clearly understand relevant rules and regulations.
Confirmation	Auditors may request the businessmen paying VAT whether they were getting VAT refund timely and as per their entitlement.
Re-performance	Auditors can compute VAT or VAT refund considering that a tax-payer has paid certain amount of VAT on sales and another amount on purchase of taxable supplies. Based on these hypothetical figures, auditors can determine the amount of VAT payable/refundable as the case may be. They can then ask the NTO to work out VAT payable/refundable using their own system and check that they agree.
Analytical Procedures	Auditors may tabulate information on VAT collected and refunded for three years and compare the figures to see if there is any abnormal change in VAT collection/refund. In case auditors see significant changes/abnormal linkages in the collection and refund, they should look for explanation. They will need to use professional judgment in arriving at a conclusion.

10.6 Evaluating Evidence

Whether sufficient appropriate evidence has been obtained on which to base the auditor's conclusion is a matter of professional judgment, which involves considering the relationship between the cost of obtaining evidence and the usefulness of the information obtained. The auditor uses professional judgment and exercises professional skepticism in evaluating the quantity and quality of evidence, and thus its sufficiency and appropriateness, to support the assurance report.

An audit is a cumulative and iterative process. As the auditor performs planned procedures, the evidence obtained may cause the auditor to change the nature, timing or extent of other planned procedures. Information may come to the auditor's attention that differs significantly from that expected and upon which planned procedures were based. For example:

- The extent of non-compliance that the auditor identifies may alter the auditor's professional;
- judgment about the reliability of particular sources of information;
- The auditor may become aware of discrepancies in relevant information, or inconsistent or missing evidence; and
- If analytical procedures were performed towards the end of the engagement, the results of those procedures may indicate a previously unrecognised risk of non-compliance.

In such circumstances, the auditor may need to re-evaluate the planned procedures.

Having gathered all audit evidence, the auditor should take the necessary steps to form conclusions. When evaluating the audit evidence, the auditor reviews documentation to

determine whether the subject matter has been sufficiently and appropriately examined. Based on the audit procedures performed and the audit evidence obtained, the auditor should evaluate whether the assessments of the risks of non-compliance or compliance deviation remain appropriate or whether they need to be revised.

The evaluation process entails considering evidence that both supports and seems to contradict the audit report, conclusion or opinion on compliance or non-compliance. If audit evidence obtained from one source is inconsistent with that obtained from another, or if there are any doubts about the reliability of the information to be used as evidence, the auditor should determine what modifications or additions to the audit procedures would resolve the matter and consider the implications, if any, for other aspects of the audit.

10.7 Forming Conclusions

While drawing a conclusion or opinion, auditors evaluate evidence in relation to identified materiality in order to identify potential instances of material non-compliance. Determining the significance of findings is based on the concept of materiality. What represents a material compliance deviation is a matter of professional judgment and includes considerations of context as well as quantitative and qualitative aspects of the transactions or issues concerned. The list below identifies some of the factors that the auditors have to consider in applying professional judgment to determine whether or not an instance of non-compliance is material.

- Importance of amounts involved (monetary amounts or other quantitative measures such as number of citizens, entities or organisations involved, pollutant emissions levels, time delays in relation to deadlines, etc.);
- Circumstances;
- Nature of the non-compliance – law, regulation or internal procedure;
- The cause leading to the non-compliance – negligence or fraudulent act;
- Possible effects and consequences non-compliance may have;
- Visibility and sensitivity of the criteria or program in question, (for example, is it the subject of significant public interest, does it impact vulnerable citizens, etc.);
- Needs and expectations of the legislature, the public or other users of the audit report;
- Nature of the relevant authorities; and
- Extent or monetary value of the non-compliance.

While evaluating audit evidence auditors consider whether material non-compliance are pervasive or not. If it is unable to obtain sufficient and appropriate audit evidence due to an uncertainty or scope limitation auditors evaluate whether it is both material and pervasive.

In evaluating their evidence, the auditors can conclude that the audit evidence is conflicting. Some evidence supports the subject matter information, and other evidence appears to contradict it. The auditors need to weigh the extent and credibility of conflicting evidence in order to determine the true situation. This is where auditors can use the hierarchy of evidence reliability, so that for example written external evidence is more credible than an informal management representation to the contrary.

After evaluating whether the evidence is sufficient and appropriate given the assurance level of the audit, the auditor should consider how best to conclude in the light of the evidence.

Auditors need to properly document all significant activities that they carry out while

gathering and evaluating evidence. They need to revise their strategy and audit plan considering the results of their work in this phase. Frequently, additional information comes to the notice of auditors that require them to relook at subject matter, criteria, scope, control/ risk assessment, and materiality consideration as explained above. Auditors may, during compliance testing, come across instances that indicate fraud risk within the audited entity. How to address the issue is explained earlier.

During this phase, auditors also need to engage with management to seek clarification on some issues that have bearing on how they are looking at subject matter, criteria, scope, audit risk, and materiality. This interaction helps auditors to make proper adjustments in their audit strategy and audit plan. Further, it also helps management to identify control weaknesses and other systemic weakness that it can begin to tackle promptly.

Chapter 11: Following Up Compliance Audits

This chapter examines: [Introduction](#); [Why Follow-up](#); [What to Follow-up](#); [When to Follow-up](#); [How to Follow-up](#); and [Decisions of the SAI](#).

11.1 Introduction

Compliance auditing guidelines recommend that auditors should follow-up instances of non-compliance when appropriate.

The auditee should have a reasonable opportunity to provide comments on any factual errors it identifies in the final audit report.

If these factual errors are accepted, the audit report will be rectified before the report or the findings in the audit report is made publicly available.

The SAI should consider the information in the final audit report and any submissions from the organisation and respond in a proportionate manner to any non-compliance identified through the audit process.

The follow-up process is one in which the compliance auditor monitors, to ascertain whether and what corrective actions have been undertaken by the responsible party in addressing instances of non-compliance identified in a previous audit report/s. In instances where this is necessary, the SAI should follow-up on its recommendations to be able to provide the intended user with an update on the responsible party's actions and initiatives taken towards compliance.

Some compliance audits can be an assessment of very specific compliance with regulations and, therefore, the attestations provided by the auditor, whether annually or periodically, are required to be very specific about whether compliance has been achieved or not. In such a case, follow up of response to reporting might not be required if the attestation is that the auditee has complied. But if the auditor identified issues, follow up could be very urgent. It could be very important that the non-compliance is not repeated for the following year, or there may be wider observations about weaknesses in surrounding systems. It is very important that the auditor considers the nature of the audit and the findings and recommendations carefully and that follow up is timely in the context of the specific audit issues and risks. Timeliness will be different in each case, and annual follow up may not be sufficiently timely to be helpful in some cases.

It should be noted that the follow-up process may not be applicable in all instances and in all SAIs. The mandate of the SAI along with the nature of the audit will determine if follow-up is applicable.

In order to promote transparency, the SAI should publish a summary of outcomes of each Audit on its website at the conclusion of the audit follow-up process.

11.2 Why Follow-up

The SAI has a role in monitoring actions taken by the responsible party in response to matters raised in an audit report. The need to follow-up previously reported instances of non-compliance would vary with the nature of the subject matter, the non-compliance identified and the particular circumstances of the audit. The follow-up process facilitates the effective implementation of corrective actions and provides useful feedback to the audited

entity, the users of the report and the auditors in planning future audits.

Follow-up serves many purposes for the three parties. These include:

- **For the responsible party:** Demonstrates the audited entity's effectiveness in addressing the issues;
- **For the intended user:** Provides an update on what has been achieved by the responsible party and the existing gaps, if any; and
- **For the auditor:** To assess the effectiveness of its work.

11.3 What to Follow-up

Follow up focuses on whether the audited entity has adequately addressed the matters raised, in a specific audit report.

Here are some examples of what to follow-up:

- Recommendations in the audit report; and
- Issues raised by intended users', example, Parliament, Public Accounts Committee or the Public.

It is important to note that the auditor may expand the scope to include other relevant aspects outside of its recommendations. The key here is to determine whether the entity complied with all the necessary directives.

11.4 When to Follow-up

The decision as to when to follow up would be based on a number of factors. If the audit was a one-off attestation engagement, then follow-up may not be necessary. However, if auditors come out with significant deviation having implications for the citizens, even the audit engagement is one off, its results should be followed up.

If the engagement is a direct engagement and is conducted at specific periods then follow-up may be necessary.

The auditor should allow the responsible party sufficient time to implement the recommendations yet still ensure that the follow-up is relevant to the intended users. As a result, the auditor would exercise professional judgment in this regard.

Some SAI may, depending on the frequency of an audit engagement, conduct follow-up procedures while performing current audits.

11.5 How to Follow-up

SAI should have established policies and procedures for conducting follow-up. The auditor should prepare an audit plan identifying the resources to be used, the recommendations and audit findings to be examined and timeframe in which to complete.

Some audit procedures that were used during the initial audit engagement may be applicable during the follow-up. The auditor should access to determine adequacy of these procedures.

Other follow-up processes may include internal reviews and evaluations prepared by the audited entity or others.

Regardless of the form, the auditor should obtain sufficient and appropriate audit evidence to support the findings and conclusions.

The follow-up report could follow the same reporting lines as the audit engagement including submission to relevant intended users.

11.6 Decisions of the SAI

The SAI may decide, based on the results of the follow-up, to continue monitoring the implementation measures of the audited entity or it may take the decision to undertake an entirely new audit engagement. In audits carried out on a regular basis, the follow-up procedures may form part of the subsequent year's risk assessment.

Chapter 12: Quality Assurance over Compliance Audits

This chapter examines: [Introduction](#); [Key Principles of Quality Control and Assurance](#); [Assigning Responsibility for Quality Control \(QC\)](#); [The Importance of Quality](#); [Quality Characteristics](#); [Quality Control](#); [Quality Monitoring](#); and [Quality Assurance](#).

12.1 Introduction

The existence of a good system of quality control is an important prerequisite for all stages of an audit. Quality control among other things has to guarantee that audits will be performed according to the adopted professional standards, that the proper methods and techniques will be applied, that sufficient work has been done to be able to give an opinion and that the gathered and evaluated evidence will substantiate that opinion. In that respect it is better to speak about “**quality assurance**”.

Senior management is responsible for a good functioning system of quality control within the SAI. It should establish policies and procedures designed to promote an internal culture recognising that quality is essential in performing all of its work. Such policies and procedures should be set by the Head of the SAI who retain overall responsibility for the system of quality control.

ISSAI #140¹⁶ provides essential guidance on this matter. It also provides a gap analysis tool to assess if the SAI meets all the relevant demands.¹⁷ The SAI should periodically apply this tool to assess if it (still) meets the standard and what steps should be taken if not. More guidance on the application of quality control in the audits can be found in ISSAI #2220.

In the Pacific there is scarce resources and staff numbers to establish a separate quality unit to conduct this. However, there are options that SAIs can undertake to ensure a quality assurance mechanism is in place. The important matter is to ensure the key principles have been considered and adapted accordingly.

Refer to PASAI’s Quality Assurance Manual for more details or guidance. However, please be aware that this manual will also be updated in the near future. Accordingly, it is recommended that you take no substantive work based on this manual but only use it for interim solutions.

12.2 Key Principles of Quality Control and Assurance

In compliance with INTOSAI P #10, the SAI should meet the following key principles for quality control and assurance:

- **Leadership responsibilities for quality within the organisation:**

Key principle: The SAI should establish policies and procedures designed to promote an internal culture recognising that quality is essential in performing all of its work. Such policies and procedures should be set;

- **Relevant ethical requirements:**

Key principle: The SAI should establish policies and procedures designed to provide it with reasonable assurance that the SAI, including all personnel and any parties contracted to carry out work for the SAI, comply with relevant ethical requirements;

- **Acceptance and continuance of client relationship and specific engagements:**

Key principle: The SAI should establish policies and procedures designed

to provide the SAI with reasonable assurance that it will only carry out audits and other work where the SAI:

- is competent to perform the work and has the capabilities; including time and resources, to do so;
- can comply with relevant ethical requirements; and
- has considered the integrity of the organisation being audited and has considered how to treat the risk to quality that arises.

- **Human Resources:**

Key principle: The SAI should establish policies and procedures designed to provide it with reasonable assurance that it has sufficient resources (personnel and, where relevant, any parties contracted to carry out work for the SAI) with the competence, capabilities and commitment to ethical principles necessary to: - carry out its work in accordance with relevant standards and applicable legal and regulatory requirements; and enable the SAI to issue reports that are appropriate in the circumstances.

- **Engagement Performance:**

Key principle: The SAI should establish policies and procedures designed to provide it with reasonable assurance that its audits and other work are carried out in accordance with relevant standards and applicable legal and regulatory requirements, and that the SAI issues reports that are appropriate in the circumstances. Such policies and procedures should include: - matters relevant to promoting consistency in the quality of the work performed; supervision responsibilities; and review responsibilities.

- **Monitoring:**

Key principle: The SAI should establish a monitoring process designed to provide it with reasonable assurance that the policies and procedures relating to the system of quality control are relevant and adequate and are operating effectively. The monitoring process should: - include an ongoing consideration and evaluation of the SAI's system of quality control, including a review of a sample of completed work across the range of work carried out by the SAI; require responsibility for the monitoring process to be assigned to an individual or individuals with sufficient and appropriate experience and authority in the SAI to assume that responsibility; require that those carrying out the review are independent (i.e. they have not taken part in the work or any quality control review of the work).

12.3 Assigning Responsibility for Quality Control (QC)

The Head of the SAI will retain **overall responsibility** for the system of quality control regardless of the system in place to ensure Quality Control. In the PASAI region, most SAI are not large enough to be able to have a dedicated team working full time on Quality Control. Accordingly, it is **recommended** that the day to day responsibility rests with a senior officer (often the Deputy Head) who should be assisted by an *ad hoc* Quality Assurance Review Committee (QARC).

The **operational responsibility** should be assigned within the team that will plan and conduct the audit on a certain entity (Financial Audit), subject matter (Compliance Audit) or programme (Performance Audit). The most logical person would be the Team Leader or Audit Manager. Before the start of the audit assignment, a quality control procedure should

be in place and it must be clear who will be performing it and how.

He/she should see to it that quality control procedures are implemented at the engagement level in order to provide reasonable assurance that the audit complies with professional standards and the applicable legal and regulatory requirements, and that the auditor's report is appropriate in the circumstances.

Under such a system, the senior officer responsible for QC should design the quality control process, to maintain it and to periodically evaluate it. He/she should also scrutinise the audit files to assess the compliance to the quality control procedures and the quality of the work performed including the quality of the conclusions.

This should be done **before** presenting the report to the auditee or after. A quality review before presenting the results to the auditee is an extra safeguard that the audit has been performed according to professional standards, that the report reflects the factual situation and that the conclusions are valid.

In terms of being a learning organisation the review could be done afterwards. The senior officer responsible for QC should give feed back to the respective audit team and also use the results for evaluation purposes.

12.4 The Importance of Quality

The SAI should have a **Quality Management Guideline** that will provide detailed guidance on the procedures of quality control and that will reflect the importance of quality. This guideline should comprise all the elements of ISSAI #2220 and more specific the ISA #220 part of it as far as they would be applicable for the public sector. Part of the guide would be the general quality management policy. This policy should at least state that:

- quality is the responsibility, and in the interest, of all employees;
- auditors must work continuously on maintaining and improving audit quality;
- as the SAI requires compliance and quality in the delivery of public services by its clients, so the SAI itself must strive to serve as a model for its clients; and
- quality procedures and processes are based on internationally recognised auditing standards and international good practices.

It is therefore the responsibility of each member of the organisation to strive for quality so that the end products of the SAI are of the greatest possible value to its clients and key stakeholders. This applies to each staff member, from front-line auditors to support staff.

The quality framework should include the following main components:

- **Quality Control:** means getting it right the first time by ensuring that quality procedures are embedded in auditing procedures;
- **Quality Monitoring:** involves an independent review of individual audits by the senior officer responsible for Quality Control (Assurance), to ensure that quality control procedures are being fulfilled effectively and in accordance with this manual and the detailed quality guidance; and
- **Quality Assurance:** involves an independent external assessment of the quality control and quality monitoring procedures set up and implemented at the SAI.

12.5 Quality Characteristics

Quality is an essential or distinctive characteristic or attribute. It is the degree to which a set of characteristics, inherent to a product, fulfils its requirements. In the case of the quality

of the different audits conducted by the SAI, the general quality characteristics include the following points.

- **Scope:** Did the audit plan properly address all issues needed for a successful and effective audit? Did the execution of the audit satisfactorily complete all the required components of the task plan? Was the report in line with the stakeholders' requirements?
- **Reliability:** Did the audit findings and conclusions truly reflect actual conditions with respect to the matter being examined? Are the conclusions on the assertions in the audit report fully supported by the data and evidence gathered in the audit?
- **Objectivity:** Was the audit carried out in an impartial and fair manner? The auditors should base their assessment and opinions purely on the facts and on proper analysis of the evidence.
- **Timeliness:** Were the audit results delivered in a timely manner? This may involve meeting a statutory deadline or delivering audit results when they are needed for a policy decision, or when they will be most useful in correcting management weaknesses.
- **Clarity:** Was the audit report clear and concise in presenting the results of the audit? This typically involves ensuring that the scope, findings and any recommendations can be easily understood by users of the audit report. These users may not be experts in the matters that are being addressed but may still need to act in response to the report's findings.
- **Significance:** How important is the matter that was examined in the audit? This can be assessed from several perspectives, such as the auditees' financial outlay and the effects of the auditees' performance on the public at large or on major national policy issues.

More characteristics concerning ethical and engagement elements of quality control named and explained in ISSAI #2220. The ethical elements reflect the demands as mentioned in paragraph 5.2.

12.6 Quality Control

Quality Control is about “**getting things right the first time**”. This is achieved by embedding quality procedures and processes into the audit work itself, at all stages of the audit: planning, fieldwork, reporting and follow-up. Prior to considering detailed quality control procedures, there are several important aspects of working practices that underpin operational quality: documentation and supervision.

Documentation involves two key aspects, audit evidence and working papers:¹⁸

- Auditors are required to obtain **sufficient and relevant evidence** to be able to draw reasonable conclusions. It is important for audit evidence to be reliable and sufficient to support the conclusions and any opinions that may be expressed; and
- **Working papers:** which are the documents that auditors prepare to record the performance of their work. Working papers should be sufficiently complete and detailed to enable an experienced auditor with no previous connection to the audit to gain a basic understanding of the work performed and conclusions reached.

Supervision is also a critical part of the process:

- The Team Leader of each audit team has a key role in this by reviewing the quality of working papers and ensuring that they have been prepared with due care and attention and are sufficient to support any conclusions drawn. They must also

¹⁸ The demands for audit documentation are specified in ISSAI #2230. In the chapters concerning audit planning, conducting, reporting and follow up, the relevant demands will be addressed.

ensure that all auditors have the necessary skills for the job at hand, that the audit guidance and programmes have been understood and that the work is carried out in accordance with those programmes; and

- Supervision is done by reviewing the working papers against a checklist and providing written comments to the auditor, covering what has been accomplished and which areas need improvement.

12.7 Quality Monitoring

Quality monitoring is the internal review function established to ensure that quality control procedures are effective. Quality monitoring covers all audit work, from the planning stage through to reporting. Within SAI an *ad hoc* QARC should be established. It should meet on a regular basis to monitor the quality of ongoing audit tasks.

The QARC should carry out its review in reference to standard checklists for the planning stage, fieldwork stage, and reporting stage. The review covers all the relevant reports and working papers and may involve interviewing members of the audit team about specific aspects of the audit.

The Committee should produce an annual report based on these individual quality monitoring reviews to form part of the SAI Annual Report.

12.8 Quality Assurance

Quality assurance is quite distinct from quality monitoring and concerns an independent “post-audit” review of the quality management arrangements, including the effectiveness of the quality control and quality monitoring procedures. It is generally achieved through a combination of internal and external reviews.

The purpose of an external review is to obtain a fully independent assessment of satisfaction of the required standards – against a regional or sectorial benchmark rather than internal expectations. This external “peer” review might be carried out by another SAI or by a commercial audit firm. At intervals of no more than five years the quality of the audits performed by the SAI has to be assessed.

The external review team will submit a report to the Head of the SAI outlining its key findings, areas for improvement, and actions required to achieve these improvements. In the future, the scope of this external assessment will be extended to include feedback from the audited bodies on how the audits were conducted and, on the benefits, gained from the audit process. The results of the assessment will be transmitted to Parliament as part of the SAI Annual Report.

PART FIVE: NEXT STEPS

Chapter 13: How to Customise and Develop your Compliance Audit Manual

13.1 Introduction

As was indicated in the introduction, this manual is designed to be a draft manual for you to develop your own manual suited to the unique circumstances of your mandate. It is accompanied by a separate volume containing a Case Study for Compliance Auditing

13.2 Process

How you customise the two volumes is up to you. However, we think that the following approach is a good basic method:

- **Customise Manual:** go through this manual and delete sections not relevant to your mandate; draft and add any new material which you consider necessary. This includes the Acronyms;
- **Pilot Audits:** test the draft volumes you produce by undertaking a number of pilot audits. Ensure that there is detailed feedback from each audit and that this is used to update the draft manual; and
- **Final Manual:** you will then have a manual which is specifically tailored to your needs and which can be used to undertake your planned audit work.

13.3 Caveat

There can be no substitute for referring to, and using, the auditing standards appropriate to your jurisdiction and following your own regulatory framework. Nothing in the manual is intended to attempt to override these; its purpose is purely to offer guidance to each SAI with a view to improving the quality of external audit in the region. This, in turn, will lead to improved governance and will benefit all the citizens of our countries.

ANNEXURES

Annex 1: Audit Programme: Ministry of Fisheries and Livestock Payroll

The payments of 'pay-roll' of the Ministry of Fisheries and Livestock should be done with compliance of the existing rules and regulations and directives of the Ministry of Finance. The benefits and other facilities provided to the employees should not be inflated or undermined. Arrear claims should be paid as per regulations.

System Objective

To ensure that the payments have been made according to the existing rules and regulations and arrear claims and other benefits are duly paid off. The budget estimation for payroll has to be justified as well.

	Details of Risk	Potential Consequences
1	Payment of inflated amounts (due to wrong pay fixation).	Irregular payment made, possibility of fraud
2	Pay roll records are not maintained properly.	Possibility of fraud
3	Payments are made to the employees with no assigned activities.	Possibility of fraud
4	Improper appointment/ ghost employees.	Cause financial loss to government, possibility of fraud
5	Payment of undue higher scale.	Cause financial loss to government, possibility of fraud
6	Inaccurate pension payment.	Cause financial loss to government, possibility of fraud

Audit Objectives

Evaluate the main controls over the 'payroll' payment entries to ensure that:

- All the payments are made with compliance to the existing rules and regulations and the directives of the Ministry of Finance;
- Payments are approved by the competent authorities;
- All the documents and vouchers are properly kept and correctly recorded;
- Proper compilation of Accounts; and
- Physical employees are paid rather than ghost employees.

Pay roll entries of the Ministry of Fisheries and Livestock

Auditee	Ministry of Fisheries and Livestock		WP Ref.		
Period Under Review	Financial Year 2020	Prepared By		Date	

Audit Test	Audit Assertion	Signed/ Date	WP Ref
Collect a detail list of pay-roll in the FY 2011 – 12 of the concerned departments and sort the list in three categories according to nature (pay-fixation, last pay certificates, arrear payments). Select random samples of size 5 from each lot (for field offices size 3) and examine the following:			
1. Determine whether payrolls are calculated accurately.	Regularity,		
2. Match gross pay with pay fixation data.	Accuracy		
3. Determine whether allowances are calculated as per government rules.	Regularity, Accuracy		
4. Match gross pay with audit register.	Occurrence Accuracy		
5. Determine whether all deductions are correctly calculated as per rules.	Regularity Accuracy, Accuracy,		
6. Determine whether gross pay and net pay are correctly calculated.	Classification, Accuracy, Cut off		
7. Verify whether there are evidences that arithmetic calculations have been checked.	Accuracy,		
8. Verify that an LPC is available for all cases selected.	Cut off,		
9. Ensure that total deductions are not greater than basic pay.	Classification,		
10. Re-calculate the pay fixation for each member of the sample and assess if the pay fixations have been correctly calculated, in accordance with Government Orders.	Cut off,		
11. Select a sample of pay-bills and check the net amount of the pay-bill against the cheque amount credited against the bank in proper time.	Completeness,		
12. Select a sample of employees and physically verify their presence/existence.	Regularity,		
13. Payments are booked in exact code and in proper period, the total payment does not exceed budgeted amount.	Accuracy		

Annex 2: Audit Programme: Funding

Funding is received from the donors and paid into the Consolidated Fund. Funding from the Centre is then sent to the field offices where it is spent.

System Objective

Funding by the donors is received in a timely manner and allocated to the correct classification/financial year and is spent in conformity with the donor wishes.

	Detail of Risks	Potential Consequences
1	Funding received from a donor and allocated to a different donor	Disclosure error on face of financial statements (one donor's figure too high and another's too low). The donors are likely to spot this (embarrassing if SAI doesn't spot it)
2	Funding received from a donor and misappropriated	As above but for one donor, illegal act, damage to reputation of government, donor would be reluctant to release more funds
3	Funding received and recorded at a lower amount	As per 2 above
4	Funding received and not recorded in a timely manner/ recorded in the wrong financial year	As per 1 above (can be for just one donor, or more)
5	Contribution of different donors not separately shown in AFS	Donors' demand not met
6	Discrepancy between field office statements and central records (mismatch)	Accounts inaccurate, 2, 3 or 4 above
7	Closing balance and Opening balance mismatch	Accounts inaccurate
8	Discrepancy between the total resources and the total expenditure	Accounts inaccurate
9	Misleading /False disclosures	Accounts inaccurate
10	Financial Statement overstated/misstated	Accounts inaccurate
11	Arithmetic errors	Accounts inaccurate
12	Untraceable expenditure / Significant amounts remain unauditible	Accounts inaccurate
13	Reconciliation of accounts not confirmed	Weakness in accounts keeping and inaccurate accounts - 2, 3, 4 above
14	Funds are allocated and accounted for on the wrong accounts head and code	Classification of accounts not followed
15	Disbursement Link Indicators (DLIs) not achieved	Donors cease to provide funding
16	Re-appropriation made but not authorised	Accounts inaccurate

Annex 3: Audit Programme: Capital Expenditure, Supplies and Services and Repairs and Maintenance (Primary Education)

Capital Expenditure, supplies and services and repairs and maintenance are made by the Director General (Programme Director) of Primary Education for the procurement of assets and equipment, supplies and services and repairs and maintenance.

System Objective

Procurement of *bona fide* assets and equipment, supplies and services and repairs and maintenance for which there is a genuine need and the amount is spent in conformity with the Public Procurement Rules and in a timely manner.

	Detail of Risks	Potential Consequences
1	Expenditure for which there was no genuine need	Overstatement of capital expenditure in the financial statements and irregular expenditure
2	Fraud / Irregular expenditure / Loss of fund/Misuse	Overstatement of capital expenditure in the financial statements and irregular expenditure
3	Without approval/ Beyond DPP provision /Questionable expenditure	Overstatement of capital expenditure in the financial statements and irregular expenditure
4	Failure to fully apply the Public Procurement Rules (PPR)/Violation of PPR	Overstatement of capital expenditure in the financial statements and irregular expenditure
5	Expenditure charged to the wrong year of account	Under or overstatement of capital expenditure in the financial statements
6	Expenditure authorised by an individual in excess of his delegated authority limit	Violation of delegation of financial powers
7	Expenditure charged to the wrong ledger code/in the incorrect account figure	Misclassification of expenditure in the financial statements
8	For capital expenditure, stock entry and distribution report of capital assets and equipment not confirmed	Fraud, violation of Government rule
9	For capital expenditure, quality of assets and equipment was low	Misuse of money
10	VAT/other taxes are paid where appropriate	Government deprived from revenue
11	For repairs and maintenance, payments in respect of non-project vehicles or overly frequent repairs in excess of need	Irregular expenditure
12	Risk that goods received are not of an appropriate quality and so represent bad value for money	Poor value for money

Annex 4: Examples of Subject Matters, Subject Matter Information and Criteria in Compliance Auditing

The criteria should be made available to the intended users and others as appropriate, for example by listing them in the auditor's report, or making reference to the criteria if they are readily available in another document.

In situations where, for whatever reason, the audit criteria are not considered suitable, the SAI will recommend that the appropriate bodies clearly formulate the general principles to be applied for public sector entities in such matters.

	Subject matter	Subject matter information	Criteria
1	Financial performance and use of appropriated funds: budget execution, including verifications that funds have been used as per with the purposes and intentions as decided by the legislature. Can be part of a regularity audit, including an audit of financial statements.	Financial information such as financial statements.	Relevant budget legislation such as an appropriations act. Approved budget.
2	Financial performance, for example revenue in the form of: project funds from donor agencies, funds from the central government, other similar types of funds and how they have been used.	Project financial information / project accounts.	Relevant legislation relating to the use of central government funds; Mandated activities of the audited entity; Funding agreement terms.
3	Financial performance, such as revenue in the form of grants, and how the revenue has been used.	Financial information related to use of the grant	Mandated activities of the audited entity. Grant agreement terms.
4	Financial performance, e.g. revenue and expenditures under a contract or loan agreement, and how those funds have been used.	Financial information related to the contract or loan agreement.	Terms of the contract or loan agreement.
5	Procurement	Financial information	Relevant procurement legislation and regulations (national and international). Terms of a contract with a supplier.
6	Expenditures	Financial information Statement of compliance	Relevant budget legislation such as an appropriations act. Other relevant legislation. Relevant ministerial directives, government policy requirements and legislative resolutions. Contractual terms.

7	Programme activities	Activity indicators or reports.	<p>Relevant agreed levels of performance such as those set out in laws and regulations, ministerial directives, goals agreed by the legislature, international treaties, protocols, conventions and agreements, a service level agreement, the terms of a contract, industry standards, and reasonable public expectations. For example:</p> <ul style="list-style-type: none"> - number of kindergarten spots in relation to the number of eligible children; - number of qualified nurses and doctors per number of citizens; - number of miles of paved roads; - number of months required to process benefits payments or building permits frequency and quality of accounting information to be provided by service organisations; - number of building inspections to be performed within a particular time period; - measurements of results related to water quality, etc.
8	Service delivery	<p>Statement of service delivery;</p> <p>Publicly reported information</p>	Relevant legislation or directives.
9	Probity of a public administrative decision	<p>Citizen complaints register;</p> <p>Publicly reported information</p>	Relevant legislation or directives.
10	Behaviour / Propriety	<p>A statement of compliance, for example a statement of independence (legal competence).</p> <p>In the public sector this statement may sometimes be implicit and related to the concepts of probity and propriety. (See criteria section.)</p>	<ul style="list-style-type: none"> - Relevant legislation or directives on the behaviour of public sector officials; - Code of ethics or internally developed code of conduct; - Stated values or leadership principles; - Internal policies, manuals and guidelines; - The organisation's terms of reference, bylaws or similar texts; - Contractual terms (e.g. agreed confidentiality or quarantine arrangements subsequent to certain employment situations).

11	Membership obligations	Statement of compliance	Agreed terms of membership
12	Health and safety processes	Statement of compliance Financial transactions	Relevant occupational health and safety legislation, e.g. in relation to access for persons with disabilities. Policies, processes, manuals, guidelines, etc.
13	Environmental protection processes	Statement of compliance Financial transactions	- Relevant environmental legislation, such as relating to water quality, waste disposal or carbon emissions levels; - Terms of international environmental treaties, protocols, conventions and agreements - Policies, processes, manuals, guidelines, etc.
14	Internal control processes	Statement of compliance. Financial transactions.	An internal control framework, for example COSO ¹⁹ , CoCo or similar, or internal control requirements set out in relevant legislation or generally accepted within a jurisdiction. Policies, processes, manuals, guidelines, etc.
15	Processes specific to the entity's activities and operations, such as the payment of pensions and social benefits, the processing of passport and citizenship applications and the assessment of fines and other forms of penal sanctions	Statement of compliance. Financial transactions.	Relevant legislation and directives. Policies, processes, manuals, guidelines, etc.
16	Physical characteristics	Specifications document or the physical object itself.	Building code (size, height, purpose, density measures for a particular zoned area, etc.). Terms of a construction contract or other type of contract.
17	Tax revenue, taxpayer obligations and other obligations involving reporting to regulatory authorities	Individual and corporate tax returns. Other tax forms submitted to regulatory authorities (such as VAT forms, reporting forms for agencies operating within regulated industries such as banking and finance, pharmaceuticals, etc.)	Relevant legislation and industry-specific codes. Tax code, revenue code or similar.

Annex 5: Examples of Audit Criteria when Compliance Audit is Performed together with the Audit of Financial Statements

The following are illustrative examples of audit criteria that may be applied when examining whether the income and expenditures of the audited entity are in compliance with authorities, including budget legislation.

Income and Revenues

1. constitutional provisions or other basic principles concerning the government's authority to impose taxes, demand fees or sell goods and services or real estate.
2. provisions of tax law determining the object of taxation.
3. provisions on the calculation of taxes, custom duties and other levies.
4. provisions on the systems and procedures to withhold and collect taxes.
5. provisions on tax control.
6. provisions and principles of budgetary, competition or other law regulating sales of goods and services or real estate by public authorities.
7. provisions and principles on the proper calculation of prices and fees.
8. budget appropriations to obtain income.
9. provisions or common practice that serves to prevent corruption and ensure that sales of goods, services and real estate are processed through transparent procedures in accordance with principles of legality and equality.
10. principles that serve to maximise revenue and prevent loss of payments.
11. provisions and principles regarding the terms of payment, the access to give credit, demand guarantees and on the collection of debts.

Operational Expenditure

1. principles that serve to ensure economy and efficiency by optimizing the number and composition of the staff.
2. provisions regulating the salaries, pension and other remuneration of staff.
3. provisions regulating the number and categories of staff that may be employed.
4. provisions and principles on reimbursement of personal expenses of staff.
5. provisions and principles of budgetary, competition or other law on the procedures of public procurements.
6. provisions and principles for acquiring goods and services.
7. principles on rights and obligations in contracts and provisions of agreements with suppliers of goods and services.
8. provisions, principles and common practice limiting the use of funds for external representation or internal staff purposes.
9. provisions and principles regarding housing rents, and rental and leasing of goods.
10. provisions and common practice regarding the procedures for processing of payments and internal controls.

Expenditure on Construction, Infrastructure, IT-systems and other large-scale investments (in addition to operational expenditure)

1. provisions in regard to feasibility studies, projecting and budgeting.
2. provisions and principles of sound management of public funds concerning public tenders and the choice of suppliers.
3. industry standards and standard contracts.
4. principles concerning contracting provisions, sound project management and budget control.
5. provisions and principles of adequate quality management in the construction/ development phase and at deliverance.
6. measures against corruption and uncompetitive behaviour.

Grants, Entitlements, Guarantees and other Financial Contributions to Enterprises, Organisations or Individuals

1. provisions on the purpose of the scheme and limits on how the funds may be used.
2. principles of equality, objectivity and transparency in the process of inviting applications and allocating grants.
3. criteria of eligibility.
4. provisions regarding accounting, control and audit of recipients.
5. conditions imposed by the administration's decisions or agreements with beneficiaries.
6. provisions on the coverage of guarantees and the conditions under which they should be paid.
7. provisions on calculation of amounts.
8. provisions on the process of payment including conditions concerning advance payments, subsequent reimbursements and/or the final settlement.

Annex 6: Examples of Sources to be used in Gaining an Understanding of the Audited Entity and Identifying Suitable Criteria

The following is an illustrative, but not exhaustive list of sources that public sector auditors may use in identifying suitable audit criteria:

- a) Laws and regulations, including the documented intentions and premises for establishing such legislation.
- b) Budgetary legislation / approved budget or appropriations.
- c) Documents of the legislature related to budgetary laws or resolutions, and to the premises or particular provisions for use of approved appropriations, or for financial transactions, funds and balances.
- d) Legislative or ministerial directives.
- e) Information from regulatory authorities.
- f) Official records of meetings of the legislature, public accounts committee or similar committee of the legislature, or other public bodies.
- g) Principles of law.
- h) Legal precedent.
- i) Codes of practice or codes of conduct.
- j) Internal descriptions of policies, strategic and operational plans and procedures.
- k) Manuals or written guidelines.
- l) Formal agreements, such as contracts.
- m) Loan or grant agreements.
- n) Industry standards.
- o) Well established theory (for example theory for which there is general consensus. Such theory may be obtained, for example, from published information such as technical literature and methods, professional journals, etc, or through inquiry with knowledgeable sources such as experts in a particular field).
- p) Generally accepted standards for a particular area (such standards are normally clearly identifiable standards that have their source in some form of legislation and that are a result of established practice and legal precedent, for example 'generally accepted accounting principles' in a particular country).
- q) For audits of propriety: Principles for sound public sector financial management and conduct of public sector officials. Principles of conduct may arise from the legislature's or public expectations regarding the behaviour of public sector officials. In some cases, these principles may be documented in only fragmentary ways. They may, in some cases, only be defined as a result of their breach.

Additional sources which public sector auditors may use to obtain an understanding about the audited entity, its environment and relevant program areas may include:

- a) The entity's annual report.
- b) Legislative propositions and speeches.
- c) Websites.
- d) Published reports, articles in newspapers or journals, other media sources, etc.
- e) Knowledge obtained from previous audits.
- f) Information gathered through meetings and other communication.
- g) Minutes of Board or other management meetings.
- h) Internal audit reports.
- i) Official statistics.

Annex 7: Examples of Factors Related to Assessing Risk in Compliance Auditing

The following are examples of factors that may be considered in assessing risk in a compliance audit. The list is not intended to be exhaustive, and the factors will depend on the particular audit circumstances.

The Audited Entity's Objective and Mandate

1. Are the audited entity's objective, mandate and legal capacity clearly stated and readily available?
2. Have there been recent changes in mandate, objectives or program areas?
3. Are program areas or relevant subject matters clearly identifiable?
4. Do program areas overlap considerably with other entities such that there is a risk of duplication or of fragmentation?

Organisational Structure

1. What is the legal basis of the entity (ministry, directorate, agency etc) and from where does it derive its authority?
2. Does the audited entity have clearly defined roles and responsibilities, and related authority attaching to these?
3. Are these roles, responsibilities and authorities clearly communicated and understood throughout the entity?
4. If the entity is part of a hierarchic structure, and another entity is responsible for supervision of the audited entity, how does such supervision take place?
5. Does the organisation focus on risk assessment and risk management, including risks of non-compliance, in its operations?
6. Have there been recent organisational changes?
7. Are any activities outsourced to other entities?
8. If activities are outsourced, how is compliance and performance monitored?
9. Are there other potential risks associated with outsourcing?
10. Do personnel have adequate competence and ethical behaviour?
11. Do personnel seek relevant information and is relevant information easily accessible?
12. Is information communicated on a timely basis in the organisation?
13. Are there any aspects of organisational structure that could give rise to greater risk of fraud?

Political Considerations

1. To which level of government does the particular entity belong and does it have relations to other levels of government?
2. What are the responsibilities (constitutional or other) of the relevant minister, or of entity management?
3. What is experience in dealing with the entity's political vs. administrative management?
4. Is there political consensus, or are differing views freely expressed?
5. How is the political management comprised?
6. What are program areas of political focus, visibility and sensitivity?
7. How does the working relationship between political and administrative management function?
8. Are there any areas of particular public interest?
9. What is experience in relation to one entity exercising unfavourable influence on other related entities in the public sector hierarchy?
10. Are there any political considerations that could give rise to greater risk of fraud?
11. Do laws and regulations contain requirements for political neutrality related to the use of resources and funds, and what is past experience in this area?

Laws, Regulations and Other Relevant Authorities

1. Is it clear which laws, regulations and authorities apply to the audited entity and the particular subject matter?
2. Are there overlaps or inconsistencies between different sets of legislation?
3. Is the entity a law-making body, and if so what impact can the law-making process have on the rights of individuals?
4. If the entity is a law-making body, has it delegated any authority to other entities, such as regulatory authorities or private sector entities?
5. Is relevant legislation relatively new, or is it well established?
6. If new, is it clear in terms of form and content such that it may be clearly understood and applied?
7. If well established, has legal precedent been consistent such that the legislation is clearly understood and applied?
8. Is the relevant program area subject to significant application of judgement in its operations?
9. If a significant amount of judgement is applied, is this done in accordance with the intentions behind the laws and regulations?
10. If a significant amount of judgement is applied, is it applied consistently?
11. Are other bodies involved in interpreting or supplementing the relevant legislation?

12. Has the entity carried out its duties on a timely basis such that individual rights have not been compromised, and there have not been significant negative financial consequences due to passiveness?
13. Have channels for complaints and appeals for affected parties been used appropriately?
14. Have any individual's / organisation's rights been compromised in any way through the entity's interpretation and application of particular legislation or regulations?
15. Are there any aspects of laws, regulations or other authorities that could give rise to greater risk of fraud?

Significant Events and Transactions

1. Are there any significant events or transactions that may give rise to significant risks or fraud risks (e.g. significant procurement contracts, long term construction contracts, dealings in financial instruments such as foreign exchange contracts, significant loans or financial speculation, privatisation etc)?
2. Does the entity possess the necessary authority and competence to enter into and carry out significant events and transactions?
3. Have experts been engaged in connection with significant events and transactions?
4. If experts have been engaged, what precautions have been taken to ensure their competence and objectivity?
5. How is the work of experts monitored?

Management

1. Is there stability in the management team or have there been changes in key personnel?
2. How are members of management recruited (open and transparent processes with real competition, or token process)?
3. Is management actively involved in assessing risk on a continual basis?
4. Has management considered the consequences of changes in the entity's environment and the impact this may have on the audited entity?
5. Is management conservative in its approach or more willing to take risks (e.g. what is the 'risk appetite')?
6. What initiatives has management taken to identify and avoid significant risks that could have an adverse impact on the entity?
7. Are risk evaluations that are performed throughout the entity effectively communicated to management at the appropriate levels?
8. Does management actively monitor and evaluate the consequences of their decisions and actions?
9. Have previous audits identified instances of non-compliance, fraud, unlawful acts, unethical behaviour, management bias, etc?
10. How does management balance the achievement of program objectives with the need to manage risk, and ensure compliance with laws and regulations etc?

Annex 8: Examples of Compliance Audit Procedures for Selected Subject Matters

This table shows illustrative examples of possible compliance audit procedures in the areas of environmental legislation and project funds from donor organisations. It is not intended to be an exhaustive list of procedures. Audit procedures must be designed for the particular audit circumstances and objectives.

Sample Audit Procedures	
Subject Matter: Environmental Legislation	
1	Obtain an overview of relevant environmental legislation to which the entity is required to adhere.
2	Inquire with management, and internal audit as applicable, as to the processes and routines in place to ensure compliance with relevant environmental legislation.
3	Review manuals and systems descriptions to understand the processes and relevant controls. Document the process and identify key controls. Test key controls as necessary.
4	Perform a media search, and other databases as applicable, to identify previous instances of non-compliance by the entity.
5	Review any inspection reports, including those of internal audit as applicable. Follow up any areas that may indicate significant risks of non-compliance with environmental legislation.
6	Confirm that the audited entity has necessary permits and registration certificates as appropriate. Evaluate procedures to ensure that these remain valid and up to date.
7	Review minutes of meetings of environmental, or health and safety committees. Follow up as necessary.
8	Interview selected staff as to their understanding of relevant policies and procedures in place, including training, and how these procedures operate in practice.
9	Inquire with management, and legal counsel as appropriate, as to any previous, existing or potential environmental liability claims. Consider the causes and effects/impacts of any such claims.
10	Observe processes and routines in practice (e.g. waste disposal – properly stored and disposed of, etc) and document appropriately (e.g. photo or video evidence may be relevant).

Sample Audit Procedures	
Subject Matter: Project Funds Received from a Donor Organisation	
1	Obtain an overview of the funding agreement and any relevant legislation, directives, mandates, etc to which the entity is required to adhere.
2	Inquire with management, and internal audit as applicable, as to the processes and routines in place to ensure compliance with the terms of the funding agreement and relevant legislation, directives, mandates, etc. Inquire as to routines to ensure appropriate accounting and disclosure.
3	Review manuals and systems descriptions to understand the processes and relevant controls related to compliance with such funding agreements. Document the process and identify key controls. Test key controls as necessary.
4	Perform analytical procedures for assessing risks, and substantive procedures as considered necessary. For example, compare any financial information, including project accounts, with budget and prior year(s). Follow up suspected deviations as necessary in the circumstances. Review project accounts for unusual or significant transactions. Follow up as necessary.

5	<p>Select a sample of transactions related to project funds. For each transaction selected, test compliance with the terms of the funding agreement and any relevant legislation, for example:</p> <ul style="list-style-type: none"> • requirements related to use of funds • proper approval and authorisation • reporting requirements • proper accounting and disclosure, including appropriate accounting policies and recording transactions in the appropriate periods, etc.
6	<p>Where project funds have been used for specific purposes, assess the need to perform physical inspections. Follow up as appropriate.</p>
7	<p>Review related correspondence, minutes of meetings etc to identify any relevant matters. Follow up as necessary.</p>
8	<p>Consider the need to obtain any written confirmations from third parties and follow up as appropriate.</p>
9	<p>Consider the need to obtain specific written representations from management in regard to the funding agreement.</p>
10	<p>Perform cut-off testing and review after the period end as necessary to ensure funds are accounted for in the appropriate period.</p>

Annex 9: Examples of Compliance Deviations

The following table provides some examples of compliance deviations and includes considerations related to materiality and forming conclusions. The comments related to materiality and forming conclusions are not intended to be definitive assessments of whether the particular example constitutes a material compliance deviation or not, but rather to highlight relevant considerations. The determination of materiality will depend on the particular circumstances and the professional judgement of the public sector auditor.

Example of Compliance Deviation		Considerations Relating to Materiality and Forming Conclusions
1	<p>During the year, a government agency received budget appropriations through the Ministry of Education for national educational purposes.</p> <p>The agency's grant expenditure for the year included \$10 million to overseas high-tech manufacturers.</p>	<p>Based on the legislation governing the government agency, the agency did not have the power to make grants to overseas bodies. The non-compliance may be material because the grant expenditure was paid out to overseas bodies and was therefore not in compliance with relevant authorities, nor was it applied to the purposes intended by the legislature.</p>
2	<p>During the year, a government agency incurred expenditures of \$100 in excess of the total expenditure of \$5000 authorised by the budget approved by the legislature.</p>	<p>In this case, actual expenditures were in excess of amounts authorised through the approved budget. This non-compliance may be material because it was a clear violation of clearly established authorities. Depending on the circumstances, including the type of expenditures, it may also be very sensitive in nature.</p>
3	<p>A citizen is entitled to a monthly pension of \$1000. The government agency has only been paying out \$900 per month. The payments were also made after the dates stipulated in the legislation.</p>	<p>Although the monetary amounts involved may not be material to the financial statements of the government agency, the consequences of the non-compliance are likely to be very significant to the individual pensioner living on a fixed income. If the non-compliance is due to a system weakness, the non-compliance may also affect many other citizens. The non-compliance may therefore be material in terms of the impact on citizens and society in general.</p>
4	<p>A single mother is entitled to monthly child benefits for each child under age 18. The government agency has paid out child benefits for a 19 year old child.</p>	<p>While this compliance deviation may have been positive for the recipient, it is not in accordance with the legislation and its intentions and may therefore be unfair to other beneficiaries. If the non-compliance is due to a system weakness, the non-compliance may also affect many other citizens. The non-compliance may therefore be material in terms of the impact on citizens and society in general.</p>
5	<p>The terms of a building code require annual inspections to be performed. The government agency has not performed inspections for the past five years.</p>	<p>The non-compliance may be significant due to qualitative aspects such as safety implications. Although no particular monetary amounts are involved, the non-compliance may be material due to the potential consequences it may have on the safety of the building occupants. In the event of a disaster, there is also a risk that the non-compliance may result in significant liability claims which could have material financial implications for the government agency as well.</p>
6	<p>The terms of a funding agreement state that the recipient of the funds must prepare financial statements and send them to the donor organisation by a certain date. The financial statements have not been prepared and sent by this date.</p>	<p>The non-compliance may or may not be material depending on whether or not the financial statements were subsequently prepared and sent, the extent of the delay, the reasons for the delay, any consequences that may arise as a result of the non-compliance, etc.</p>
7	<p>Significant system weaknesses were identified in relation to revenues collected in accordance with a tax code. The weaknesses were due to incorrect interpretation of the tax code by the audited entity. Numerous instances of taxpayers being assessed more than they were obligated to pay were identified.</p>	<p>This type of compliance deviation relates to the due process rights of individual citizens. Certain citizens were being assessed too much tax, while others were not being assessed at all. Depending on the circumstances, and because it involves a system weakness, the deviation may be both material and pervasive, in which case an adverse opinion on compliance would be appropriate.</p>

Annex 10: Example of a Compliance Audit “Short Form” Report

The format of compliance audit reports may vary depending on a number of factors, such as the mandate of the SAI in the specific matter being audited, relevant legislation, reporting practices or the complexity of the issues being reported. However, there is a set of minimum requirements to be met in order to present reporting formats that are consistent and understandable by the users. This will allow for a clear presentation of the work performed, the conclusions reached and identification of any unusual circumstances.

This example is an audit to see if the body we are auditing had complied with the terms of its funding.

Compliance Audit Report by the Head of the SAI

[Appropriate recipient, e.g. Organisation XYZ]

Report on [Government Agency ABC’s Compliance with the Terms of the Funding Agreement with Organisation XYZ dated xx.xx.20XX]

We have audited [government agency ABC’s compliance with the terms of the funding agreement with organisation XYZ dated xx.xx.20XX as set out in the project accounts for the year ended 31.12.20XX, showing total expenditures of \$xxx,xxx.xx].

Management’s Responsibility

According to [the terms of the funding agreement with organisation XYZ dated xx.xx.20XX], the management at government agency ABC is responsible for [preparing complete project accounts in compliance with the terms of the funding agreement].

Auditor’s Responsibility

Our responsibility is to independently express a conclusion on [the project accounts] based on our audit. Our work was conducted in accordance with the [INTOSAI Fundamental Auditing Principles and Guidelines for Compliance Audit]. Those principles require that we comply with ethical requirements and that we plan and perform the audit so as to obtain reasonable assurance as to whether [the use of the project funds are in compliance, in all material respects, with the terms of the funding agreement dated xx.xx.20XX].

An audit involves performing procedures to obtain sufficient, appropriate evidence to support our conclusions. The procedures performed depend on the auditor’s professional judgment, including an assessment of the risk of material non-compliance, whether due to fraud or error. The audit procedures performed are those we believe to be most appropriate to the circumstances. We believe that the gathered audit evidence is sufficient and appropriate, such as to form a basis for our conclusions.

Report on Other Legal and Regulatory Requirements

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

[In some jurisdictions, the auditor may have additional responsibilities to report on other matters that are supplementary to the auditor’s responsibility to express an opinion on the financial statements, as described in ISA 700, paragraphs 35-36 and A37-A38.]

Report on Compliance

[Note: The form and content of this part of the audit report will vary with the circumstances and depending on the SAI's mandate and other reporting responsibilities].

Management's Responsibility for Compliance

In addition to the responsibility for the preparation and presentation of the financial statements described above, management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.

Auditor's Responsibility

In addition to the responsibility to express an opinion on the financial statements described above, our responsibility includes expressing an opinion on whether the activities, financial transactions and information reflected in the financial statements are, in all material respects, in compliance with the authorities which govern them. This responsibility includes performing procedures to obtain audit evidence about whether the agency's expenditure and income have been applied to the purposes intended by the legislature. Such procedures include the assessment of the risks of material non-compliance. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion on Compliance

In our opinion, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them.

[Include responses from the audited entity as appropriate, for example after the Opinion paragraph, in summary under a heading 'Responses from the Audited Entity,' or as a separate appendix]

[Include constructive recommendations as appropriate, for example after the Opinion paragraph, in summary under a heading 'Recommendations' or as a separate appendix]

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

Conclusions

Based on the audit work performed, we found that [government agency ABC's use of project funds received from organisation XYZ] is in compliance, in all material respects, with [the terms of the funding agreement dated xx.xx.20XX].

[Responses from the audited entity as appropriate, for example in a summary under a heading of "Responses from the Audited Entity" or as an appendix]

[Recommendations as appropriate, for example under a heading of "Recommendations" or as an appendix]

Annex 11: Example of a Qualified Opinion

This example reflects a situation where there has been non-compliance with the authorities' requirements, in particular with relevant legislation and with the purposes and intentions of the legislature, and where the auditor has determined that the effects are material but not pervasive. The introductory sections of the report and the sections after the compliance opinion are the same as in the example in Annex #10.

[appropriate introductory sections of the report]

Audit Report

[appropriate introductory text]

Basis for Qualified Opinion

During the year, government agency ABC received budget appropriations through the Ministry of Education for national educational purposes. My audit revealed that grant expenditures for the year included \$10 million to overseas high-tech manufacturers.

Based on *[the legislation governing the audited entity]*, government agency ABC did not have the power to make grants to overseas bodies. The grant expenditures paid out to overseas bodies were not applied to the purposes intended by the legislature and are therefore not in compliance with the requirements of the authorities that govern it.

Opinion on Compliance

In my opinion, **except for** the expenditures paid to overseas bodies as described in the Basis for Qualified Opinion above, in all other material respects the activities, financial transactions and information reflected in the financial statements are in compliance with the requirements of the authorities that govern them.

[appropriate concluding sections of the report]

Annex 12: Example of an Adverse Opinion

This example reflects a situation where there has been non-compliance with the authorities' requirements, in particular with relevant legislation and with the purposes and intentions of the legislature, and where the auditor has determined that the effects are both material and pervasive. The introductory sections of the report, and sections after the opinion, are unchanged from the example in Annex #10.

[appropriate introductory sections of the report]

Audit Report

[appropriate introductory text]

Basis for Adverse Opinion

During the year, government agency ABC paid out social welfare benefits totalling \$500 million. Pension payments accounted for 90% of the total welfare benefits paid out. The financial statements fairly reflect the amounts paid out. However, weaknesses identified in the controls surrounding the computer systems used to make pension payments revealed that the payments were not being made on a timely basis in accordance with *[Relevant social welfare legislation, regulations, etc.]*. The consequence of this weakness may be a violation of the legal rights of eligible pensioners.

Opinion

In my opinion, because of the significance of the matter discussed in the Basis for Adverse Opinion, the activities, financial transactions and information reflected in the **financial statements are not in compliance** with the requirements of the authorities that govern them.

[appropriate concluding sections of the report]

Annex 13: Example of a Disclaimer

This example reflects a situation where the auditor has not been able to obtain sufficient, appropriate audit evidence in regard to expenditures being in compliance with the authorities' requirements, in particular with relevant legislation and with the purposes and intentions of the legislature, and where the auditor has determined that the effects are both material and pervasive. The introductory sections of the report and the sections after the opinion are the same as in the example in Annex #10.

[appropriate introductory sections of the report]

Audit Report

[appropriate introductory text]

Basis for Disclaimer

During the year, government agency ABC received budget appropriations through the Ministry of Education for national educational purposes. Our audit revealed that grant expenditures for the year, as reflected in the financial statements, included \$10 million to a private research institution. This grant accounted for 90% of total grant expenditure for the year.

The evidence available to me for determining whether the grant expenditure was paid out in accordance with *[Relevant legislation, regulations, etc.]* was limited. Due to hurricane damage, government agency ABC was unable to provide sufficient documentation to demonstrate that the private research institution was eligible to receive such grants. There were no other satisfactory procedures I could carry out to determine if the payments were paid out in accordance with relevant legislation and were therefore applied to the purposes intended by the legislature.

Disclaimer

Because of the limitation of scope described in the Basis for Disclaimer above, **I am unable to form an opinion** as to whether the activities, financial transactions and information reflected in the financial statements are in compliance with the requirements of the authorities that govern them.

[appropriate concluding sections of the report]

Annex 14: Example of an Emphasis of Matter and Other Matter(s) Paragraph

In some situations, there may be a need to elaborate on particular matters that do not affect the compliance opinion. An Emphasis of Matters or Other Matters paragraph is used in such circumstances as illustrated in the following example. The introductory sections of the report and the sections after the compliance opinion are the same as in the example in Annex #10.

[appropriate introductory sections of the report]

Audit Report

[appropriate introductory text]

Opinion

In my opinion, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the requirements of the authorities that govern them.

Emphasis of Matter

I draw the reader's attention to Note xx attached to the financial statements. This note explains the uncertainty related to the pending legal decision regarding the agency's interpretation of the requirements of the environmental legislation dated xx.xx.20xx. My opinion has not been qualified in respect of this matter.

Other Matter

I draw the reader's attention to the agency's compliance with the procurement legislation dated xx.xx.20xx, in force for agency ABC's jurisdiction. The terms of this legislation are contradictory to the terms of the procurement legislation dated yy.yy.20yy, which is being implemented for all jurisdictions that are parties to the ZZZ general trade agreement. This includes agency ABC's jurisdiction. There is a need for the legislature to give this matter further attention such that the necessary amendments to the procurement legislation dated xx.xx.20xx may be enacted to bring the two texts into alignment.

[appropriate concluding sections of the report]

Annex 15: Compliance Audit Letter of Engagement

[Name of Auditee]

[Insert Address of Auditor]

[Insert Address of Auditee]

Subject: Letter of engagement regarding the compliance audit of [Insert Name of Entity]

Reference:

Sir,

1. INTRODUCTION

1.1 The purpose of this letter is to set out the basis on which the Supreme Audit Institution (SAI) audits the [Insert details of activities being audited] of the [Insert Name of Entity] and the respective responsibilities of the Secretary of the [Insert Name of Entity] as Accounting Officer and the Head of the SAI, acting on behalf of the SAI. This engagement will be conducted with the sole objective of our expressing an opinion on [Insert Name of Entity]'s compliance with [Insert details of legislation or other regulations that govern the activities being audited].

The terms of the audit engagement are set out below. This letter will remain effective until a new audit engagement letter is issued.

2. SCOPE OF THE AUDIT

2.1 The compliance audit will be conducted in accordance with the International Standards for Supreme Audit Institutions (ISSAI) [or other standards – insert as necessary] and will cover the [Insert details of activities being audited] for the [Insert Name of Entity] for the financial year [Insert Financial Year].

3. RESPONSIBILITIES OF THE SAI

3.1 The SAI audits the [Insert details of activities being audited] under [insert legislation] which states that [inset details of powers].

[Please also include details of any other rules, laws and regulations applicable to the scope of the compliance audit.]

3.2 Consequently, the Head of the SAI is responsible for reporting whether in his opinion the [Insert details of activities being audited] of [insert name of entity] are, in all material respects, in compliance with the authorities which govern them. This responsibility includes performing procedures to obtain audit evidence about whether the expenditure and income have been applied to the purposes intended by the legislature.

Such procedures include the assessment of the risks of material non-compliance.

4. THE COMPLIANCE AUDIT PROCESS

4.1 The audit will be conducted in accordance with the International Standards of Supreme Audit Institutions (ISSAI) [or other standards]. These Standards require that we comply with ethical requirements and plan and perform our audit to obtain reasonable assurance of detecting errors, irregularities and illegal acts.

4.2 We shall obtain an understanding of the accounting and internal control systems to

assess their adequacy as a basis for the preparation of the **[Insert details of activities being audited]** and to establish whether proper accounting records have been maintained by the **[name of entity]**. We shall expect to obtain such appropriate evidence as we consider sufficient to enable us to draw reasonable conclusions therefrom.

4.3 The nature and extent of our procedures will vary according to our assessment of the **[Insert name of entity]** and, where we wish to place reliance on it, the internal control system, and may cover any aspect of the operations that we consider appropriate.

4.4 Limitations of a Compliance Audit

4.4.1 We will plan our audit so that we have a reasonable expectation of detecting material instances of non-compliance with relevant rules, laws and regulations in relation to the **[Insert details of activities being audited]** including those resulting from fraud, error or non-compliance with laws or regulations, but our examination should not be relied upon to disclose all areas of non-compliance as may exist. Due to the test nature and other inherent limitations of compliance audit there is an unavoidable risk that some material misstatement may remain undiscovered.

4.4.2 Our work on internal control will not be sufficient to enable us to express any assurance on whether or not the **[Insert name of entity]** internal controls are effective. Our audit of the **[Insert details of activities being audited]** cannot be relied upon to draw to your attention all matters that may be relevant to your consideration as to whether or not the system of internal control is effective.

4.5 MANAGEMENT REPRESENTATIONS

As part of our audit process we will request from management written representations on matters material to the **[Insert details of activities being audited]** where other sufficient appropriate evidence cannot reasonably be expected to exist, and where management may have made certain oral representations (Letter of Representation).

4.6 RELIANCE ON THIRD PARTIES

4.6.1 Use of Experts

Where we judge that it is appropriate to use the work of an expert we will:

- obtain sufficient appropriate audit evidence that such work is adequate for the purposes of the audit;
- evaluate the professional competence of the expert;
- evaluate the objectivity of the expert;
- ensure that the scope of the work of the expert is adequate for our purposes; and
- evaluate the appropriateness of the expert's work as audit evidence regarding the assertions being considered.

4.7 COMMUNICATIONS

4.7.1 At the start of our audit, we may issue an Audit Plan, containing details of identified risks and planned audit work on the **[Insert name of entity]** for the coming year. This will detail where the audit team intends to make use of other auditors or experts.

4.7.2 At the end of each audit we will report formally to you on:

- Any significant weaknesses in, or observations on, the accounting and internal control system including areas of non compliance with applicable authorities;

- Errors and instances of non compliance with relevant rules, laws and regulations identified in the course of the audit (unless deemed clearly trivial);
- Uncorrected misstatements;
- Expected modifications to the audit report; and
- Any other matters of interest.

5. CLIENT RESPONSIBILITIES

5.1 Our audit will be conducted on the basis that the Secretary **[Insert name of entity]** and those charged with governance acknowledge and understand that they have responsibility for:

(a) For such internal control as the Secretary **[Insert name of entity]** and those charged with governance determines is necessary to enable compliance with applicable rules, laws and regulations; and

(b) To provide us with:

- Access to all information of which the Secretary **[Insert name of entity]** and those charged with governance are aware that is relevant to our audit such as records, documentation and other matters;
- Additional information that we may request for the purpose of the audit; and
- Unrestricted access to persons within the entity from whom we determine it necessary to obtain audit evidence.

6. AUDIT ARRANGEMENTS

6.1 Access to Data and Personal Data

As part of our audit work we may need access to personal data which the **[Insert name of entity]** holds.

6.2 Health and Safety

Members of the audit team will be in touch with relevant **[Insert name of entity]** to discuss practical arrangements and the timing of audit visits. However, we would appreciate your co-operation in relation to the provision of support for our employees covering health, safety and emergency arrangements applicable to your premises.

6.3.2 The **[Insert name of entity]** is also responsible for the controls over, and the security of their website. The examination of the controls over the maintenance and integrity of the **[Insert name of entity]**'s website is beyond the scope of our audit.

7. OTHER MATTERS

7.1 Use of Report and Confidentiality

Any formal report or other unpublished reports from us may not be provided to third parties. Such consent will be granted only on the basis that such reports are not prepared with the interests of anyone other than the **[Insert name of entity]** in mind and that we accept no duty or responsibility to any other party as concerns the reports.

7.2 Quality of Service

We would like to provide you at all times with a high-quality service to meet your needs.

If at any time you would like to discuss with us how our service to you could be improved,

please raise the matter immediately with me.

ACCEPTANCE:

8.1 Once agreed, this arrangement will remain effective for future years unless it is terminated, amended or superseded. Should you wish to discuss any aspects of this before signing at the foot of this letter and returning a copy, please do not hesitate to contact me.

Yours Sincerely,

Head of SAI

Date:

Annex 16: Audit of Donor Funded Projects

Objectives and Scope

The objective of donor funded projects audits is to conduct an audit of revenues and expenditures in accordance with the project's agreements, compliance with projects agreement, and a review of the project's internal controls.

The specific objectives of this audit are to:

- Express an opinion on whether the project's financial statements present fairly, in all material respects, resources received from donor agency and expenditure incurred for the periods under audit in conformity with International Accepted Accounting Standards which are compatible with the donor agency's requirements;
- Determine if the expenditures reported as incurred under the project's agreement are in fact allowable, and reasonable;
- Evaluate and obtain sufficient understanding of the internal control structure, assess control risk, and identify reportable conditions, including material internal control weaknesses and prepare a management letter reporting important weaknesses and findings;
- Perform tests to determine whether projects implementation unit complied, in all material respects, with the project agreement terms and applicable laws and regulations; and
- When the auditors are carrying out performance audit of a donor-funded project, they should comment on the economy, efficiency, effectiveness and equity in the use of resources, achievement of the planned results of the project/programme.

Planning Stage

Generally, certification audit programmes will cover project expenditure (e.g. bill paying) but some separate check may be necessary for overseas aid receipts control. Having regard to the above, there is also a case for periodic Performance Audit (PA) examinations of aid funded operations. This could take the form of a broad study supported by a close examination of one or two individual projects.

The main features of such a PA study will be to examine the adequacy of control over development projects with the following questions in mind:

- are projects conceived in relation to national needs along with state funded projects. Ideally, a programme of projects important to national development will be drawn up. Then, some of these will be selected for overseas funding. It should not be the case that the aid donor suggests the project. (i.e. there should be an integrated budgetary system regardless of input source);
- are forecasts prepared of support costs (including loan repayment charges), future cost implications and foreign exchange needs;
- are the objectives and benefits clearly defined and subject to technical analysis, evolution and consideration of alternatives;
- is there a central planning document which includes financial authorities, powers of project officers, project timetables and reporting requirements of donor countries;
- is there a rigorous system for control over land procurement, award and execution of contracts, both physically and financially, and over stores procurement;
- are there arrangements for timely claiming of funds;

- are there procedures for reviewing progress against target dates, for evaluating project outturn against original feasibility study, for employing performance indicators to measure unit costs, etc. and for assessing the effectiveness of the provision (including a review after, say, twelve months); and
- is there provision for prompt preparation of the project accounts?

Having assessed the adequacy of control procedures, in the light of inquiries along the lines suggested above, the auditor can then test compliance by reference to the standard of performance in practice.

The objective of this phase will be to produce an approved strategic and comprehensive audit plan to cover the year under audit. The following tasks should be performed:

- Carry out a **detailed review** of the project operations and activities and, and the environment in which the project conduct its operations. The auditors should acquire knowledge of the project/programme by reviewing all the applicable documents such as:
 - The agreements between donor and recipient;
 - The sub-agreements between the recipient and other implementing entities, as applicable;
 - Contracts and sub-contracts with third parties, if any; and
 - The budgets, implementation letters and written procedures approved by the donor.
- Conduct **specific assessments** of individual audit areas as required by the donor agency audit requirements;
- Conduct a **preliminary understanding** of the projects internal controls including computer controls (when applicable) for the purpose assessing associated audit risks;
- Conduct **preliminary analytical procedures** to identify where potential errors or problems may exist and take significant fluctuations into consideration in determining the extent of substantive testing.;
- Prepare audit plan and identify **detailed audit procedures**. In particular, the auditors should:
 - establish audit criteria and the tests necessary to meet them;
 - identify the important aspects of the environment in which the project is being undertaken;
 - develop an understanding of accountability relationship between the donor and the recipient;
 - consider the form, content and users of audit opinions, conclusions or reports;
 - identify key management systems and controls and their strengths and weaknesses;
 - determine the materiality of matters to be considered;
 - review internal audit of the project and its work programme;
 - determine the most efficient and effective audit approach;
 - provide for appropriate documentation of the audits plan of the project;
 - prepare a budget and a schedule for audit; and
 - familiarise the audited entity about the scope, the objectives and the assessment criteria of the audit and discuss them as necessary.

It is necessary that SAI should agree with responsible Government Agency (normally Ministry of Finance) that they are completely informed on donor agreements in order to have an adequate picture of their potential workload.

Execution Stage

At the execution stage, the auditors should ensure fulfilment of the audit objectives. The financial audit will consist of the following procedures:

- **Perform Compliance Tests:** to ensure compliance with the agreements signed between the receiving country and the donor;
- **Perform Substantive Testing:** and other audit procedures on transactions recorded by the project accounting system;
- **Perform Detailed Analytical Procedures:** on the financial data to identify situations requiring modifications of the audit plan or accounts that may contain misstatements and likely to be adjusted;
- **Provide Supervision:** during the fieldwork to ensure that audit objectives are achieved and the audit is completed with minimum disturbance to the project operations; and
- **Prepare a Management Letter:** including audit findings and recommendations and receive management response on those

A financial/performance audit of the funds provided by the donor shall be performed in accordance with the INTOSAI Standards, or other approved donor guidelines where applicable, and accordingly includes such tests of the accounting records as deemed necessary under the circumstances. Some of the procedures which are emphasised by donors include:

- The auditors should **review procurement procedures** to determine whether sound commercial practices including competition were used, reasonable prices were obtained, and adequate controls were in place over the qualities and quantities received;
- The auditors should ensure that all funding received by the recipients from donor was **properly recorded** in the recipient's accounting records and that those records were periodically reconciled with information provided by donor;
- The compliance review should determine if cost **sharing contributions were provided** and accounted for in accordance with the terms of agreement. The auditor's report on compliance should set forth, as findings, all material instances of noncompliance;
- The auditors should review the **cost sharing schedule** and determine whether cost sharing **contributions** were provided and accounted for by the recipient in accordance with the terms of the agreements; and
- The auditors should **review the status of actions taken on findings and recommendations** reported in prior audits of donor-funded programmes.

Reporting Stage

In carrying out audit of donor-funded projects, SAI should follow reporting guidelines on audit reports, timing and format, with copies sent to implementing agency. The objective of the final phase will be to finalise the audit report per the donor agency reporting requirements.

This will entail the following steps;

- Carry out a **final review** of the fieldwork to ensure that:
 - all the work has been completed and documented properly,
 - all audit recommendations are supported by examples and management response has been obtained, and;
 - all agreed audit areas have been covered.
- Prepare a **draft report** in compliance with donor agency auditing requirements; and
- Conduct **final working paper reviews and finalise audit reports**.

The auditor's report should state in proper perspective, material irregularities, illegal acts or other non-compliance. To give the reader a basis for judging the prevalence and consequences of these conditions the instances of irregularity or illegal acts identified should be related to the number of cases examined and be quantified, if appropriate, in monetary terms.

The reports should also contain, after each recommendation, pertinent views of responsible recipient officials concerning the auditor's findings and action taken by the recipient to implement the recommendations. If possible, the auditors should obtain written comments.

When the auditors disagree with management comments opposing the findings, conclusions or recommendations, they should explain their reasons following the comments. Conversely, the auditors should modify their report if they find the comments valid.

Annex 17: Auditing Gender Equity

[Source: INTOSAI Development Initiative Performance Audit Handbook]

NB Although the examination of Equity is the new 4th “E” of Performance Auditing – see the new manual – as this topic is one of Social Responsibility Auditing it has been included here.

1. Planning Framework: Gender Equity

Gender-Based Analysis (GBA) is a lens of analysis that examines and assesses existing differences between women’s and men’s socio-economic realities and life situations. It also analyses the differential impacts of proposed and existing policies, programs, legislative options, and agreements on women and men. The use of GBA as an analytical tool is critical in designing legislation, policies, regulations, programs, or projects. GBA is a management tool that can be examined by auditors and that can also be used as an audit tool.

Gender-Responsive Budgeting (GRB) is a government planning, programming, and budgeting process that contributes to advancing gender equality and fulfilling women’s rights in particular. It entails identifying and reflecting needed interventions to address gender gaps in sector and local government policies, plans, and budgets. GRB also aims to analyse the gender-differentiated impact of revenue-raising policies and the allocation of domestic resources and official development assistance.

Gender-Responsive National Development Plans and Sectorial Plans have been developed by more than 40 countries to take into account the importance of unpaid work in households and how it factors into the overall economy. The Gender and Work Database, an online research tool, provides extensive information about work and employment as they relate to gender and other social factors.

2. Auditing Equity

Equity audits are essentially “social audits” that consider whether government policies, internal practices and related support systems to mainstream socially disadvantaged segments/groups are effective, reinforce each other and are being implemented. These audits practices focus on stakeholder participation [i.e. participation of rights holders (people) and duty bearers (government or service providers)] and accountability.

Auditors examine all facets of a given subject matter (i.e. a policy, a programme or an institution) in order to determine whether gender is incorporated adequately and appropriately into objectives and targets, project design, implementation, monitoring and evaluation, in order to ensure outcomes and policies align with higher level objectives on gender.

Ideally, an equity audit focuses on both the programme and the organisation but it could focus on one or the other. So the audit can be roughly divided into two groups: questions about programme, policy objectives and implementation and more internally focused questions on the organisation, i.e. capability of the organisation to address equity issues, organisation culture etc. The audit examines the relative progress made in mainstreaming issues of the target group and helps to build organisational ownership for equity/equality initiatives and sharpens organisational learning.

2.1 Importance of Performance Audit on Gender Equity/Equality

There are several reasons why it is important to examine gender equity or equality through a

performance audit:

- To determine the degree of implementation of national and international commitments to gender equity or equality, including legislation, policy, and action plans;
- To identify and examine the gender-specific impacts of government programs, operations, administration, and financing; and
- To make recommendations that can lead to improvements in the design, implementation, and results of government policy and programming, contributing to better gender equality outcomes.

2.2 Audit Process: Addressing Equity and Equality

In order to provide a practical understanding of how concepts of social inclusiveness, equality and equity can be addressed through a performance audit, the following sections illustrate on “**gender equality**” in relation to different audit phases.

Although significant progresses have been made in both developed and developing countries to address the inequalities between women and, girls and boys, but it has been demonstrated clearly that gender equality matters needs to be addressed further both as a core development objective and as a means to increase economic growth and development. Goal 5 of the SDG specifically looks at gender equality and women empowerment. Therefore, as more governments are carrying out gender responsive programmes supported by improved legislation, policy making and funding, audits of gender equality/equity are becoming more and more imperative.

2.3 Audit Topic Selection and Definition

As we know, the first step in the performance audit cycle is to select a topic. The importance of gender equality may influence audit topic selection. SAIs are encouraged to apply a “gender lens” to their strategic planning process and related activities such as area watching, scanning the public sector environment, and discussions with external stakeholders. In effect, this involves assessing individual entities and programs as well as government-wide initiatives to determine if gender equality is relevant and significant.

Each of these situations could influence whether the entity or programme will be selected for a gender equality audit and, if so, the focus and type of audit approach that will be adopted.

2.4 Audit Planning

Determining whether gender equality issues should be included in the scope of an audit is a crucial decision to be taken during the planning phase. In some cases, gender equality may be an explicit component of the audit topic, for example where the organisation is delivering a gender equity program. In other cases, a focus on gender equality may be less apparent, and may be achieved through routine management activities that foster gender equality in public sector entities and programs.

2.4.1 Developing Audit Questions

Depending on the explicit or implicit nature in which gender equality is being addresses, the auditor can develop questions about programme, policy objectives and implementation and/ or more internally focused questions on the organisation, i.e. capability of the organisation to address equity issues, organisation culture etc. Following there are some examples of questions that could be used on gender audits.

Questions for Overall Government

- Has the government endorsed the UN Convention for Elimination of Discrimination against Women?
- Has the government developed a Policy or legislation related to gender equity or equality?
- Does the government require a Gender-Based Analysis of policies, legislation, programs and budgets?

Questions for Individual Programmes or Government Entities

- Has management issued a policy or strategy that clearly articulates its commitment to gender equality?
- Is there communication to ensure employees, service providers, and beneficiaries are aware of the policy or strategy?
- Has senior management provided a clear mandate and authority to a person(s) or group in terms of program delivery, coordination, assessing results, and reporting?
- How are gender issues mainstreamed into programme implementation?
- Has the entity established an operational plan to achieve gender equity or equality?
- Has the plan established baseline data, performance indicators, or targets relating to gender equality issues?
- Are operational plans supported by appropriate information and data analysis?
- Does the organisation use gender-based analysis to support policy decisions and funding requests? Does it integrate the results of such analyses into policies and programmes?
- Does the organisation track program budget, inputs, outputs, and outcomes using sex-disaggregated data?
- Do program managers collect and provide the required performance information related to gender equality?
- Does the organisation report on its gender equality program, activities, and initiatives?

2.4.2 Assessing Risks: Indicators that Gender Equity is at Risk

During the planning phase, auditors may come across information or situations that suggest that the achievement of gender equality is at risk in a given program or entity. The following are some potential **indicators that gender equality is at risk**:

- A gender-based analysis has not been conducted or insufficient attention is paid to completed analyses;
- Policy or programme design and implementation do not consider gender issues;
- An approved programme has no financial or technical resources dedicated to the design and implementation of a gender equality strategy or plan;
- Personnel have not been trained in gender equality issues both in internal administration and programme delivery options;
- Barriers to achieving gender equality still exist;
- There is no mechanism to allow staff to raise gender-based issues;
- The organisational culture does not stress the need for gender equality; and
- For a gender equality programme, standards of service are not met.

2.4.3 Relationship of Gender Equality to Program Efficiency, Economy, and Effectiveness

In determining the audit focus, the auditor also needs to consider the “3 Es”. Specifically, the auditor has to decide which of the 3 Es – economy, efficiency, or effectiveness – the audit is primarily concerned with. This drives the audit objective and associated criteria as well as the evidence required to reach conclusions against the objectives.

- A performance audit that is primarily concerned with whether the government’s intended gender equality outcomes, goals, and targets are being realised suggests a focus on effectiveness;
- An audit that is primarily concerned with how resources and processes are used to achieve intended output or outcomes suggests an emphasis on efficiency; and
- An audit that is primarily concerned with how program resources are acquired (people, assets, funding) suggests a focus on economy.

2.4.4 Deciding on the Audit Approach

SAI can use a system, result, or problem-oriented approach, or a combination thereof for the audit. During the planning phase of an audit, auditors are encouraged to gain an understanding of the system and processes in place to achieve gender equity/equality. This understanding will help the auditor to focus the audit on the most significant aspects.

In a system-oriented approach audit of gender equality, the focus is on the management systems, practices and internal controls used by an organisation to achieve, maintain, demonstrate, and improve the gender equality aspects of its services or operations.

In practical terms, this approach means examining the policy framework, human resource management, performance measurement and reporting systems, and management’s systems for benchmarking organisational performance. In a result-oriented approach audit, the focus is on determining whether a programme or activity is achieving intended gender equality outcomes. Generally, this involves comparing current or recent performance against benchmarks, a baseline, or key performance targets.

Systems and results are inter-related. During the planning phase, if results are not being achieved, this may suggest a weakness in underlying systems and processes. Even if intended results are being achieved, the auditor may wish to examine systems and processes to ensure that results will be consistently and sustainably achieved. Alternatively, if systems and processes are found to be robust but intended results are still not being achieved, this may cause the auditor to investigate other underlying causes or problems.

3. Examples

OAG Canada 2015 – Implementing Gender-Based Analysis

What was examined

Whether the selected departments performed adequate gender-based analysis to inform government decisions, and whether Status of Women Canada and the relevant central agencies (the Treasury Board of Canada Secretariat and the Privy Council Office) appropriately supported the implementation of gender-based analysis throughout the federal government.

Why we did this audit

Because it can help the government assess progress made to implement gender-based

analysis, in keeping with its goal of meeting its international commitments to gender-based analysis and its obligations to gender equality.

What we concluded

That the selected departments have not always adequately performed gender-based analysis (GBA) to inform government decisions. As in 2009, gender-based analysis has not been implemented in some federal departments and agencies. Furthermore, the departments that had implemented a GBA framework did not always conduct complete analyses, and the quality of their analyses was not consistent.

We also concluded that since 2009, Status of Women Canada, the Treasury Board of Canada Secretariat, and the Privy Council Office made progress in supporting the implementation of gender-based analysis throughout the federal government by providing assistance, guidance, and training. Despite these efforts by Status of Women Canada and the central agencies, barriers (such as the absence of mandatory requirements for gender-based analysis across government) prevent departments and agencies from embedding gender-based analysis in the development of their policy, legislative, and program initiatives.

OAG Uganda 2015 – Mainstreaming Gender and Equity in the Formulation and implementation of the National Budget

What was examined

Gender budgeting is a practice/ approach of allocating resources taking into consideration the different needs, interests and constraints of women and men. It involves an analysis and understanding of the situation of different categories of men and women, boys and girls to determine the gender gaps/ inequalities and setting appropriate interventions in development plans and budgets to address them.

In Government, Gender and Equity Budgeting is spearheaded by the Ministry of Finance, Planning and Economic Development (MoFPED), which aids the strengthening of the technical capacity for Gender and Equity mainstreaming in Budget and Budget monitoring processes across Government.

We assessed the extent to which MoFPED, in collaboration with Local Governments and MDAs, mainstreams gender and equity issues during formulation and implementation of the National Budget.

Why we did this audit

Gender budgeting is one of the ways of gender mainstreaming in development processes and it is about equality of access to public sector expenditure. Gender responsive budget initiatives can be carried out at various levels of public intervention be it government, civil society or in the private sector and in different domains which may cover the overall budget or selected parts.

What we concluded

There is inadequate capacity for implementing gender and equity budgeting within the MoFPED, MDAs and LGs. MoFPED needs to ensure that its officers trained in gender and equity budgeting do actually gain practical competences for implementing gender and equity budgeting. LGs also need to have their theoretical and practical competences for gender and equity budgeting built. In addition, there is need for closer collaboration amongst MoFPED, MoGLSD and LGs in the implementation and monitoring of gender and equity budgeting.

Annex 18: Environmental Auditing

Planning Stage

Background

- The legal mandate of the entity;
- The entity's approach to environmental issues and the environmental management system;
- Laws and regulations governing the environmental responsibilities;
- The existence of environmental assets and liabilities and any changes which may have occurred during the financial period under review;
- The environmental issues in the entity's industry in general;
- Any reports issued by regulatory agencies that may have a material impact on the entity;.
- Any initiatives to prevent, abate or remedy damage to the environment or to deal with conservation of renewable and non-renewable resources; and
- Any history of penalties or legal proceedings pending with regard to compliance with environmental laws and regulations.

Criteria

During the planning stage, the SAI should consider the criteria against which the audited entity's disclosures or performance will be assessed. Depending on the audit objective, the SAI should consider the following possible sources of criteria:

- Mandatory standards issued by an authoritative standard-setting body;
- Standards issued by some other recognised body either nationally or internationally;
- National and international agreements such as treaties with other jurisdictions and other United Nations conventions; and
- Performance measures of effectiveness, efficiency or economy that are prescribed by law, or specified in the official government policy for the activity.

The SAI should seek to obtain the entity's agreement to the criteria before the audit is begun. However, in seeking agreement, the SAI should take care to ensure that its independence is not compromised as a result of omitting or modifying criteria against its better judgement.

Resources Requirements

The SAI has to consider the following:

- specialist staff (who and when);
- external experts;
- travel requirements (for field visits); and
- time and cost budgets.

Execution Stage

The methods used for carrying out the environmental audit will depend on the objectives of the audit identified during the planning stage.

A regularity audit will need to assess the completeness and accuracy of figures reported.

The auditor should apply established professional national and international accounting and auditing standards. These set out the principles underlying the treatment of costs, assets and liabilities in financial statements that would apply to the treatment of environmental costs and liabilities. The SAI can apply these standards in judging the need for disclosing environmental impacts on costs, liabilities and assets in Government financial statements.

The SAI may need to audit estimates of the extent of such costs and liabilities. The auditor:

- Should consider both the actual and potential costs and impacts of environmental issues;
- Will need to confirm existing and likely changes to the or other requirements, the technology to be applied and the costing used in the estimates; and
- Will need to reach a judgement on the reliability of assumptions used in for predicting future costs, liabilities and asset values, and the accuracy of the calculations.

A performance audit with an environmental focus can often be classified as one of five specific types:

- **Auditing Government Monitoring of Compliance With Environmental Laws:**
In many countries, a lead environmental department (or other agency of the executive government) is charged with ensuring that environmental laws are properly implemented by public and/or private entities.

These laws may charge the environmental department with such activities as:

- issuing permits which for example limit the quantity or concentration of pollutants discharged;
- monitoring dischargers' compliance with such permits;
- monitoring environmental conditions to help identify other potential breaches of regulations;
- helping in the interpretation of regulations, and providing other assistance to regulated entities to assist in their compliance efforts; and
- taking enforcement actions when violations occur.

In some cases, these environmental regulatory responsibilities may be delegated by the federal (national) government to lower levels of government. In addition, other types of executive government departments (such as transportation or agriculture) may also exercise certain environmental regulatory responsibilities.

The SAI is often charged with examining how well these other departments exercise their environmental responsibilities.

Since the actual audit will depend on the nature of the audited body and the objectives it is difficult to prescribe specific steps. However, the following should be common for typical audits.

- Audits of systems for monitoring compliance with environmental laws typically begin with clear and explicit audit criteria, which are often contained in specific statutory requirements or in the lead environmental department's regulations

- implementing those statutory requirements;
 - The SAI then develops a methodology that assesses the performance of the department (or other pertinent parties) against the established criteria; and
 - Obtain agreement of methodology from lead department being audited especially for complex audits.
- **Auditing the Performance of Government Environmental Programmes:** a Government may be enabled by statute or other authority to carry out (or fund other entities to carry out) a range of other programmes or activities to achieve objectives whose principal aim is to protect or improve the environment.

Such a programme or activity may be the responsibility of a government department with a particular interest in the environment – such as a Department for the Environment having a programme to conserve sites of particular ecological importance or a Department for Agriculture through a programme for assisting farmers to adopt practices which minimise pollution.

Typical Audit Steps

- Identify environmental programmes from Government plans and annual reports or from a single Environmental Plan and Report if it exists;
- Identify the international agreements on environmental matters to which the Government has agreed, and then identify what programmes have been established to achieve them. (At the XV INCOSAI, it was decided that INTOSAI should encourage the SAIs to co-operate where possible in auditing their respective countries' compliance with international environmental accords. At the same time, it was also decided that INTOSAI should encourage the SAIs to carry out joint or concurrent audits. The INTOSAI issued guideline titled, "How SAIs may co-operate on the audit of international environmental accords" which can be referred to when carrying out such audits.);
- Consider whether to focus attention on one main policy instrument or on many different policy instruments;
- Examine the effectiveness of the programme or activity in achieving the impact;
- If desired to look at that angle, examine the economy of administrative practices to be employed and the efficiency of the utilisation of resources involved;
- Identify ways to compare the programme's arrangements to best practice or similar environmental practices in the same country or elsewhere; and
- The SAI could also report the programme's arrangements over time against the programme's own targets or targets or benchmarks set by experts.

In some cases, the Government might be required to prepare periodic reports on its environmental programmes. The SAI under those circumstances could audit the quality of the report instead reporting directly on performance.

- **Auditing the Environmental Impacts of Other Government Programmes:** in addition to programmes whose principal aim is to protect or improve the environment, all activities affect the environment in some way through their use of resources or their consequences for the area in which they are conducted. Government activities are no exception.

The environmental impacts of the activities can be highlighted as part of a wide-ranging performance audit – of the economy, efficiency, effectiveness and equity

of a Government activity – or as a narrowly defined study focusing solely on the environmental impacts.

The SAI could also focus its audit on the effectiveness of the environmental policies and programs. Some Government programmes have significant impacts – which may be positive and negative, intended and unintended. For example, the primary objective of road building is to facilitate movement of people or goods. But building a road has a secondary and direct impact through its land use and its effect on the ecology of the area and the landscape, whilst use of the road also has an impact on air and noise pollution. In a case like this it might be desirable especially for developing countries to push for programmes which improve the infrastructure than to seek environmentally friendly programmes at all costs.

Typical Audit Steps

- SAI can start by familiarising itself with any commitments the Government has made in identifying impacts for itself;
 - Review the Government’s own impact assessment (if any) and the methods used by the Government for the impact assessment;
 - The SAI may wish to test for itself the impacts the Government activity has on the environment. This can be done through discussions with experts or using other evaluation methodologies; and
 - Views of key stakeholders and academics specialising in the relevant areas could also be sought.
- **Auditing Environmental Management Systems:** organisations are introducing environmental management systems to ensure that they are systematically setting policies for continual improvement in environmental performance and are achieving the policy objectives.

Voluntary accreditation schemes have been introduced nationally, regionally, and internationally to enable organisations to obtain external confirmation of the adequacy of their environmental management systems and recognition that they are operating such systems.

The International Standard for Environmental Management Systems, ISO 14001, identifies the following features of best practice:

- Setting an environmental policy;
 - Planning— taking account of environmental aspects and legal and other requirements; and setting objectives and targets and introducing environmental management programmes;
 - Implementing and operating— establishing structures and responsibilities, training staff and communicating the main requirements; documenting the environmental management systems; operating the systems; and preparing emergency plans;
 - Checking and taking corrective action— monitoring and measurement; identifying non-compliance and taking action; and auditing the environmental management system; and
 - Management review of all aspects of the system.
- **Evaluating Proposed Policies and Programmes:** some SAI may be called upon to provide information on proposed policies or programmes to their legislatures.

This may occur, for example, where a national legislature re-focuses its attention from the question, *“Is the programme operating in conformance with its statutory requirements?”* to the more basic question, *“Do the underlying statutory requirements themselves need modification to make the programme more cost-effective or to improve it in other ways?”* Under these circumstances, it may request the SAI to analyse alternative proposals under consideration.

Generally, such work poses both challenges and risks. In particular, analyses of proposed policies or programmes may sometimes require skills outside those normally associated with auditing disciplines. For example, assessments of the cost and benefits of proposed environmental regulations often require the skills of an economist. In such situations, the SAI may need to hire individuals with the requisite skills, or it may find it more cost-efficient to seek the services of an outside consultant.

A third alternative may be to convene a panel of experts. Such panels, which may include experts from industry, government, and environmental organisations, have been used by some SAIs to help in identifying environmental audit priorities, developing audit approaches on specific issues, and collecting information.

Even with these added skills, the nature of such analyses does carry additional risks to the SAI, particularly if it is viewed as taking sides in debates over matters of policy. The SAI may consider the following alternatives to minimise such risks if it is asked to provide information on alternative policy directions:

- Provide factual information rather than judgements;
- It is less controversial, and more in line with the traditional roles of SAIs, to provide factual and analytical information on the impacts of alternative policy directions rather than recommend a specific alternative action;
- Identify consensus among experts;
- A consensus of expert opinion on a complex or controversial proposal can provide valuable support for an SAI’s conclusions and recommendations; and
- Evaluate and comment on analysis of other organisations.

It is often risky for the SAI to evaluate proposed policy alternatives if its analyses involve speculative assumptions about such matters as future rates of economic growth, or about technical factors such as how ecosystems respond to various pollution-related stresses. However, other organisations often perform these analyses, and typically report their methodologies and underlying assumptions along with their findings. Rather than having to defend its own assumptions (and potentially leaving itself open to the criticism that its assumptions were made subjectively), the SAI may find it more useful to evaluate these other studies’ assumptions, findings, and conclusions.

- **Auditing Of Policy Formulation:** the SAI can perform an audit of the policy. This could include ensuring that the correct process is followed. It should be noted that a number of SAI are specifically forbidden by their mandates to carry out such audits.

An audit of environment policy formulation could include the following:

- checking for an ambiguity; and
- ensuring conformity to national policy and international agreements.

Reporting

The format of the report will differ depending on the nature of the audit. Please refer to the appropriate audit manual for the format to apply.

Annex 19: Payroll Audit

Supreme Audit Institution

MINISTRY/DEPARTMENT: _____

DATE OF REVIEW: _____

Recurrent Expenditure - Payroll Checklist

Control Objective: To appraise approved procedures and see that they are followed; that the payments made are correct and in accordance with agreed scales; that records maintained are adequate and accurate; and that proper security is exercised over collection, make-up, custody and pay-out of cash or cheques.

Instructions: Answers to all questions to be by way of a tick (√) in the Yes/No column with comments as required.

	Yes	No	Comments	Schedule Number
1. Appointment and History Records				
1.1 Is the post within the approved establishment?				
1.2 Is posts grade and rate of pay properly authorised?				
1.3 Did the appointment follow recognised procedures?				
1.4 Does the employee hold a second position? If so, ensure that this is properly authorised.				
1.5 Does the data held on the payroll computer system agree that held manually on the individual's staff record?				
1.6 Is a permanent record kept of all service of every individual for pension and redundancy purposes?				
2. Gross Pay Calculations				
2.1 Is the grade correct?				
2.2 Is the current rate of weekly/monthly pay correct?				
2.3 Have all additional payments been properly authorised and calculated?				
2.4 Is a satisfaction record of overtime kept within the department?				
2.5 How much overtime was paid in the last three months? What percentage of normal pay for the same period is this?				
2.6 Are there satisfactory time-keeping and attendance records in the department?				

3. Deduction and Net Pay				
3.1 Have all deductions due actually been made and were they are correctly assessed and calculated?				
4. Subsidiary Records				
4.1 Have all advances and loans, which will be repayable on leaving the service, been properly recorded in the appropriate subsidiary record?				
4.2 Does the service for pension purposes, and any contributions made, recorded on the personnel record agree that in the Pension Department's records?				
4.3 Do the total tax, levy etc. deductions on the final payroll figure agree those of the receiving authority?				
5. Sickness				
5.1 Is a proper record kept of all absences through sickness?				
5.2 Have any sickness payments made been correctly calculated and recorded?				
6. Payments of Wages/Salaries				
6.1 Where paid in cash has: <ul style="list-style-type: none"> (a) The payroll been signed with the employees normal signature or thumb print? (b) The paying officer properly certified the payroll? (c) An adequate record of unclaimed wages and their disposal been kept? (d) Adequate security over the cash been exercised at all times? 				
6.2 Where paid by cheque, is the paid cheque in order?				
6.3 Is any pay sent to home addresses? If so, examine the reasons for this and confirm the accuracy of the address.				
6.4 If paid by bank credit, does the amount recorded on the payroll record agree the debit on the bank statement?				
7. Leave				
7.1 Are there adequate records for absence on annual or special leave?				
7.2 Was the annual leave taken in accordance with entitlement and was any special leave correctly authorised?				

8. Training				
8.1 Is a record kept of all absences on post-entry training? If so, has it been kept updated?				
8.2 Is a record kept of all payments with regard to training on an official training record?				

Subject to the satisfactory resolution of any major points noted in the audit report, in my opinion we have met the overall audit objectives.

Signed

Date

Annex 20: Payment of Creditors

Supreme Audit Institution

MINISTRY/DEPARTMENT: _____

DATE OF REVIEW: _____

Recurrent Expenditure - Payment of Creditors Checklist

Control Objective: To ensure that all payments made are in respect of goods received and services rendered to the organisation and that these have been properly ordered.

Instructions: Answers to all questions to be by way of a tick (√) in the Yes/No column with comments as required.

	Yes	No	Comments	Schedule Number
1. Control Systems				
1.1 Are all goods and services received adequately covered by official documentation (LPOs etc.)?				
1.2 Are all invoices paid authorised in accordance with policy and do adequate procedures exist for the control of payments where no official order is issued?				
1.3 Is there adequate control over the raising of, amendments to and deletion of standing periodic payments?				
1.4 Is there adequate control over the allocation and usage of creditors' reference numbers?				
1.5 Is there adequate control over the reconciliation of expenditure totals, invoice batch totals and cheque list totals?				
1.6 Is there adequate division of duties in order to obviate the inclusion of "dummy" invoices?				
2. Invoice Payment Records				
2.1 Is invoice certification in accordance with laid down procedure?				
2.2 Are invoices paid supported by copy orders, goods received or returned notes, or other approved form of official documentation?				
2.3 Does approved authorisation exist for raising and amending periodic payments?				
2.4 Is there any undue delay between the payment of invoices and recovery of credits?				
2.5 Are cash settlement discounts being taken where appropriate?				

2.6 Is the cost coding of invoices correct and does it agree with expenditure records?				
3. General Points				
3.1 Do controls exist to cover payments resulting from internally raised documentation?				
3.2 Is there adequate control over unused cheque forms?				
3.3 Are there adequate controls over special or quick manual payments?				
3.4 Are there adequate controls over payments against duplicate invoices?				
4. Internal Control				
4.1 Is there adequate systems of internal check with proper controls and division of duties?				
4.2 Are there lists of approved signatories?				
4.3 Is there periodic review over all unprocessed invoices?				
4.4 Are all paid invoices stamped "paid" or otherwise cancelled?				
4.5 Was there an unspent budget allocation available when the order was placed?				
4.6 Were Tender Board regulations followed, where appropriate?				
4.7 Where appropriate, have received goods been recorded on bin cards or other stores record?				
4.8 Is it possible for purchased items to be borrowed? If so, is the control over this adequate?				

Subject to the satisfactory resolution of any major points noted in the audit report, in my opinion we have met the overall audit objectives.

Signed

Date

Annex 21: Cash Control

Supreme Audit Institution

MINISTRY/DEPARTMENT: _____

DATE OF REVIEW: _____

Government Revenue - Cash Control Checklist

Control Objective: That the procedures for the security, collection, receipting and recording of all cash are adequate and in accordance with procedures; that all cash is correctly banked without delay; and that the system for posting to the correct accounts is sound.

Instructions: Answers to all questions to be by way of a tick (√) in the Yes/No column with comments as required.

	Yes	No	Comments	Schedule Number
1. Control Systems				
1.1 Do the systems provide for control over all types of receipts?				
1.2 Does the system ensure the adequate recording of all monies, received from all sources?				
1.3 Does the system provide for the prompt banking of collections on a daily basis?				
1.4 Is there adequate division of duties within the cash section?				
2. Receipt Control, Cash Control and Banking				
2.1 Is there adequate control over the stocks and issues of manual receipts?				
2.2 Is there adequate control over the daily usage of manual receipts?				
2.3 Has cash receipted from each different source been correctly recorded?				
2.4 Have all collections, including cheques, been banked without delay?				
2.5 Are all cashier's overs and shorts reported to management for action, where necessary?				
2.6 Is the system for credit posting adequately controlled?				
2.7 How is any unposted/unidentified cash recorded and posted?				
3. Security				
3.1 Can overnight cash holdings be reduced by making use of night safe facilities?				
3.2 Does the amount of cash banked warrant consideration of using contract security services?				

3.3 Can payments be made from collections? If so, are these adequately documented?				
3.4 When cash is paid from one officer to another, confirm that the hand-over regulations are adequate and are followed?				
4. Internal Control				
4.1 Are stocks and use of manual receipts independently controlled or reviewed? If so, by whom?				
4.2 Is every receipt issued to a collector accounted for?				
4.3 Is there daily reconciliation of collections and banking?				
4.4 Does the system isolate unbanked income from the previous day and ensure it is seen to be banked?				
4.5 Are all cheque payments identified on both receipt and bank paying-in slip to prevent teeming and lading?				
4.6 Does the system provide for the "crossing" of cheques, postal orders, etc. when received?				
5. Imprest Applications, Facility Accounts, etc.				
5.1 Is the annual Imprest Application prepared in accordance with Treasury Instructions?				
5.2 Are monthly requests for cash made in time and for the actual requirements?				
5.3 Is a realistic payments calendar, distributing cash disbursements on an even basis, where possible, maintained?				
5.4 Are drawings from facility accounts properly regulated?				
5.5 Are cash balances with banks kept to the minimum?				
5.6 Are inoperative bank accounts reviewed on a regular basis and, where appropriate, closed?				
5.7 Are all advances from imprests subsequently repaid and settled?				
5.8 Are all imprest accounts closed at the year end and the balances settled with the Treasury?				

Subject to the satisfactory resolution of any major points noted in the audit report, in my opinion we have met the overall audit objectives.

Signed

Date

Annex 22: Land and Buildings Register

Supreme Audit Institution

MINISTRY/DEPARTMENT: _____

DATE OF REVIEW: _____

Land and Buildings Register - Checklist

Overall Objective: To ensure that the department is utilising its land and buildings efficiently and identify any surplus to requirements.

Instructions: Answers to all questions to be by way of a tick (√) in the Yes/No column with comments as required.

	Yes	No	Comments	Schedule Number
1. Land and Buildings Register				
1.1 Do financial regulations require a land and building register to be kept?				
1.2 If so, does the head of the establishment have a copy of the instructions relating to land and buildings?				
1.3 Inspect all land and buildings which the department has. Is there any indication of under occupation of either land or buildings?				
1.4 If sites are not fully occupied, could re-arrangement of the departments operations free up land, buildings or parts of buildings for use by other departments or for disposal?				
1.5 Has management ever undertaken a review of its use of land and buildings? If so, when? Obtain a copy of the report and verify its findings and whether any action was taken on its conclusions.				

Subject to the satisfactory resolution of any major points noted in the audit report, in my opinion we have met the overall audit objectives.

Signed

Date

Annex 23: Stocks, Stores and Supplies

Supreme Audit Institution

MINISTRY/DEPARTMENT: _____

DATE OF REVIEW: _____

Stocks, Stores and Supplies - Checklist

Overall Objective: To ensure that there is an effective stock management system operating.

Instructions: Answers to all questions to be by way of a tick (√) in the Yes/No column with comments as required.

	Yes	No	Comments	Schedule Number
1. Security				
1.1 Were you asked to show any identification prior to access?				
1.2 Is there a controlled access point?				
1.3 Do the premises seem secure against intruders?				
1.4 Can storekeepers observe all exits? If not, is any improvement possible?				
1.5 Is the storekeeper the only key holder? If not, list the other key-holders.				
1.6 Is the storekeeper the only person allowed to receive and issue stores? If not, give details.				
1.7 Is there adequate control over the goods inwards bay to prevent pilfering by visiting delivery people?				
1.8 Is it possible for unauthorised persons to collect goods from the dispatch bay?				
1.9 Can control over either bay be improved? If yes, give details.				
1.10 Is the store and its contents adequately insured for loss?				
2. Fuel				
2.1 Does the storekeeper control vehicle fuel stocks?				
2.2 Are fuel pumps and inlets locked when not in use?				
2.3 Do drivers sign for fuel issues?				
2.4 Are vehicle registration numbers recorded on issue sheets?				
2.5 Are fuel pump meter readings recorded on issue sheets?				

2.6 When were the pumps last checked for accuracy of quantity delivered and recorded?				
2.7 Is dipping done at regular intervals by a person other than the storekeeper?				
2.8 Are tolerance levels allowed? If so, specify.				
2.9 Are statistics of level of issues prepared?				
2.10 Do these show the trend of issues you would expect? Is this reviewed regularly?				
2.11 Are there adequate arrangements for recharging any other authorised users?				
3. Ordering				
3.1 Are official orders used in all cases?				
3.2 Are verbal orders permitted in an emergency? If so, does the system ensure that written confirmation follows the next working day?				
3.3 Is the person signing the orders: (a) Authorised to do so? (b) Independent of the storekeeper?				
3.4 Does the storekeeper initiate requisitions for orders?				
3.5 Does the storekeeper get a copy of the order?				
3.6 Are orders issued only to approved suppliers in accordance with buying policy?				
3.7 Are they within the authorised limits?				
3.8 Are the net prices obtained the lowest possible? If no, list other deciding factors (e.g. delivery date).				
3.9 How often are suppliers asked to tender?				
3.10 Who interviews salesmen wishing to supply stock items?				
3.11 Are maximum/re-order/minimum levels of stock laid down?				
3.12 Are these levels regularly reviewed?				
4. Receipts				
4.1 Are all deliveries checked before acceptance to: (a) Delivery Notes?; (b) Copy Orders?				
If not, is the delivery note marked "subject to a detailed check"?				
4.2 Are all bulk materials weighed before being accepted, or is an official weigh ticket produced?				
4.3 Is the system for part deliveries adequate?				

4.4 Are goods received notes produced?				
4.5 Are all goods promptly recorded and taken into store?				
4.6 Is the recording of goods received independent of the checking of invoices?				
4.7 Is the person certifying the invoice as to goods received: (a) Authorised to do so?; (b) Independent of the storekeeper?				
4.8 Are there adequate procedures to ensure: (a) Return of goods to suppliers? (b) Claims for shortages, breakages and incorrect deliveries? (c) All credit notes received? (d) Return and control of chargeable containers, etc.?				
5. Issues				
5.1 Are requisition/issue notes completed for all issues being made?				
5.2 Are requisition/issue notes correctly made out and authorised by persons who are not storekeepers?				
5.3 Are requisition/issue notes examined for reasonableness of quantities? If so, (a) By whom? (b) At what stage?				
5.4 Is there a list of persons who are authorised to sign requisitions/issue notes?				
5.5 Does the storekeeper know who is authorised to sign requisitions/issue notes?				
5.6 Does the recipient sign for all items received?				
5.7 Are all bulk materials weighed before issue?				
5.8 Are the procedures in respect of unfulfilled requisitions/issue notes satisfactory				
5.9 Are arrangements for "emergency" or "night shift" issues adequate?				
6. Returns/Transfers				
6.1 Are goods returned notes used for: (a) Unused items?; (b) Second-hand items?; (c) Scrap?				

6.2 Does the person who authorises the issues make out a goods returned note? If no, detail.				
6.3 Does the storekeeper acknowledge the receipt of items returned?				
6.4 Are second-hand stores kept separate from new items?				
6.5 Are transfers between stores properly documented?				
6.6 Are goods returned promptly recorded and taken into store?				
6.7 Is the level of returns unduly high?				
7. Sales				
7.1 Are sales allowed?				
7.2 Are sales restricted to particular items?				
7.3 Are sales restricted to certain categories of persons? If so, are sales made only to those categories of person?				
7.4 Are the sales properly documented?				
7.5 Is the government's policy of charging being followed?				
7.6 Are sales prices adequate to ensure no financial loss to the government?				
7.7 Are competitive tenders invited for the sale of scrap?				
7.8 Is cash received/sale authorised by a person independent of the storekeeper?				
7.9 Does the storekeeper ensure that the payment is received and the sale authorised before the goods are issued?				
8. Accounting Records				
8.1 Where stores records are posted from prime documents, are there arrangements to ensure that all such documents are accounted for?				
8.2 Is the ledger updated at intervals not greater than those laid down by management?				
8.3 Are adequate measures taken to ensure that the ledger shows an up-to-date position?				

8.4 Are the procedures for dealing with the following satisfactory from the point of view of authorisation and correct recording: (a) Additional new stock items (including allocation of commodity codes)? (b) Deletion of stock items? (c) Adjustment of prices? (d) Adjustment of units of issue? (e) Adjustment of minimum/maximum stock levels? (f) Adjustment of re-order quantities?				
8.5 Are items of small value: (a) Treated as consumable? (b) Listed? (c) Reviewed at regular intervals?				
8.6 Is there any duplication of manual and computer records? If so, give details.				
9. Stocktaking				
9.1 Is stocktaking carried out independently of the storekeeper/stores control check?				
9.2 Are all stock checks supported by stock taking sheets?				
9.3 Are stocks checked: (a) Continuously? (b) At set intervals?				
9.4 Are all items checked at least once every year?				
9.5 Are attractive, portable and valuable items: (a) Checked at least monthly? (b) Not subject to abnormally high shortages?				
9.6 Are all discrepancies investigated and reported on? If so, by and to whom?				
9.7 Are all write-offs properly authorised?				
9.8 Is the ledger adjusted for discrepancies immediately the authority to do so is given?				
9.9 Is the control of the disposal of obsolete items adequate?				
9.10 Are tenders invited in appropriate cases for the disposal of such items?				

10. Management Information				
10.1 Does the system provide for: <ul style="list-style-type: none"> (a) Information on slow moving/ obsolete items at regular intervals? (b) Review of maximum/minimum and re-order levels? (c) Details of stock levels held on comparative dates? 				
10.2 Is appropriate action taken on the management information produced?				
10.3 In respect of the procedural manual: <ul style="list-style-type: none"> (a) Is there one? (b) Have all staff got copies? (c) When was it last reviewed? 				

Subject to the satisfactory resolution of any major points noted in the audit report, in my opinion we have met the overall audit objectives.

Signed

Date

Annex 24: Capital Scheme Investigation

Supreme Audit Institution

MINISTRY/DEPARTMENT: _____

DATE OF REVIEW: _____

Capital Scheme Investigation - Checklist

Overall Objective: To ensure that there is an effective system in place to control all stages of a capital scheme.

Instructions: Answers to all questions to be by way of a tick (√) in the Yes/No column with comments as required.

	Yes	No	Comments	Schedule Number
1. PRE-DESIGN INVESTIGATION				
1.1 Assessment of General Need				
1.1 Re-examine the original justification. Was the original data correct? What is the current data? 1.2 Is the “need” based on national policy or recommendations? If so: <ul style="list-style-type: none"> • Who made the recommendations? • On what basis are they made? • Were they set at a time of economic optimism? • Do the recommendations apply to this organisation? 				
1.3 Is the “need” based on local surveys? If so: <ul style="list-style-type: none"> • Was the survey soundly designed? • Was it properly conducted? • Have the results been properly analysed? • Is the interpretation of the results reasonable? 				

<p>1.4 Has the “need” been based on anything else? If so, what:</p> <ul style="list-style-type: none"> • strong political influence? • pet project of Head of Department? • status? • experimental project with strong board influence? 				
1.2 Having identified the “need”, why has this particular method of satisfying the need been chosen?				
<p>1.5 What alternative methods of meeting the needs have been considered?</p> <p>1.6 What alternative methods should be considered?</p> <p>1.7 Why have these alternatives been rejected?</p>				
<p>1.8 How has the level of provision been determined? Why isn’t it bigger? Why isn’t it smaller?</p>				
<p>1.9 Given the general level of provision, is the specific level at the optimum, given the capacity of staff per number of clients?</p>				
<p>1.10 Why is the project located at the proposed site? Why isn’t it located elsewhere?</p>				
<p>1.11 What have been the problems with a similar provision in the past?</p>				
<p>1.12 Does the project involve any new concepts in style of provision? If so:</p> <ul style="list-style-type: none"> • what are they? • what are the implications for costs compared to traditional methods? 				
<p>1.13 Are the estimated running costs reasonable?</p>				
1.3 Information given to Technical Officer				
<p>1.14 Does the service department have firm ideas on its requirements?</p>				
<p>1.15 Is the brief given to the Technical Officer explicit in its requirements? Does it contain:</p> <ul style="list-style-type: none"> • site? • design concept? • capacity? • services required? • scope for expansion? • scope for alternative uses: <ul style="list-style-type: none"> - present and future? - day and night? - winter and summer? 				

1.16 Apart from the brief, have there been any other communications between the service department and the Technical Officers?				
1.17 Are communications adequate?				
1.18 Does the Technical Officer appear to have a full understanding of the service department's requirements?				
1.19 Has the brief been given to the Technical Officer in sufficient time for him to prepare a design to meet the requirements of the brief?				
2. EARLY DRAFT DESIGN INVESTIGATION				
2.1 Energy Conservation				
2.1 Has use been made of any computer programs to obtain optimum conservation?				
2.2 Allowing for restrictions of the site, I the building orientation such as to maximise solar gain? For example: <ul style="list-style-type: none"> • do main doorways face south? • are doors located away from the prevailing wind? 				
2.3 If the site is exposed is a shelter belt of trees incorporated?				
2.4 Has the maximum use been made of solar panels?				
2.2 Building Techniques				
2.4 Does the draft design include any new building techniques or materials? If so: <ul style="list-style-type: none"> • are they government approved? • how long have these techniques been in existence? • how many of the organisation's buildings use the technique? • should the organisation use new techniques within (say) 10 years of introduction? 				
2.5 What are the implications for fire resistance?				
2.6 What is the extent of pre-design test drilling?				
2.3 Landscaping				
2.7 Will the intended landscape be expensive to maintain? For example: <ul style="list-style-type: none"> • roses to prune rather than low shrubs? • awkwardly shaped grass areas? • numerous grass verges to trim around trees, paths and roads? 				

2.8 Is the layout of the roads and car parks reasonable? For example: <ul style="list-style-type: none"> • is there sufficient car parking space? • is there too much car parking space? • will delivery vehicles have access and space to turn round? 				
2.4 Existing Users				
2.9 Consult users of existing buildings. <ul style="list-style-type: none"> • what are the particular problems? • does the proposed building get over these? • does the proposed building raise new problems? 				
2.10 Does the service accountant or auditor have any comments?				
3. EXAMINATION OF PROPOSED FINAL DESIGN AND ASSOCIATED BILL OF QUANTITIES				
3.1 Energy Conservation				
3.1.1 Heat/Air Conditioning				
3.1 What is the main source of fuel?				
3.2 What type of heating system is proposed?				
3.3 Is there to be one large boiler or several smaller ones?				
3.4 How has the capacity of the boiler been determined?				
3.5 Will access to the boiler be easy for maintenance and replacement?				
3.6 Is zonal heating incorporated to allow differential use?				
3.7 Are optimum start boiler controls incorporated?				
3.8 Is a frost damage prevention over-ride included?				
3.9 Are all adjustable components sealed (e.g. room thermostats)?				
3.10 Is there provision for dealing with heat on south facing glass in summer (e.g. blinds)?				
3.11 Is reflecting material specified behind radiators on external walls?				
3.12 Is a warning device included to tell of consumption in excess of the maximum demand tariff level?				
3.1.2 Ventilation and Insulation				
3.13 Is ventilation to be natural or mechanical? Why? If mechanical, is a heat recovery system included? If natural how have the openable areas been determined?				
3.14 How has the size of the glazed areas been determined?				

3.15 Is draught proofing or all doors and windows specified?				
3.16 Are door closers specified?				
3.17 Is mastic specified for all external joints around doors and windows and between building slabs?				
3.18 Is a warning light or time switch included in the controls for extractor fans?				
3.19 Why are the extractor fans there?				
3.20 Is lagging specified for all water tanks and pipe runs?				
3.21 What will be the U-value? (i.e. heat flow through the structure?)				
3.22 What will be the costs and benefits of increasing roof insulation or introducing cavity wall insulation?				
3.1.3 Water Conservation				
3.23 Will overflow pipes create a nuisance when operating?				
3.24 Are Supa taps, spray taps and non-concussive taps specified where appropriate?				
3.25 Are automatic water regulators specified for urinal slabs?				
3.26 Are spray nozzles specified for showers or the more wasteful 100mm or 150mm diameter roses?				
3.27 How has the size of the water meter been determined?				
3.1.4 Lighting				
3.28 Roof lights might be more expensive than permanent electric lighting; are any specified?				
3.29 Will light be wired parallel to windows?				
3.30 Will there be a high ratio of switches to lighting points?				
3.31 Are automatic controls envisaged?				
3.32 How has the number of lighting points been determined?				
3.2 Vandalism				
3.33 What features invite vandalism?				
3.34 What features will discourage vandalism?				
3.35 Have any of the following been considered? <ul style="list-style-type: none"> • patchwork pattern on external walls to discourage spray paint? • many smaller windows instead of fewer large ones? • wall lights positioned out of normal reach? 				
3.36 Will the design discourage the spread of fire?				
3.37 Have fire retardant paints and materials been specified?				
3.38 Are toilet cisterns concealed?				
3.39 Are hand basins flush with the walls?				

3.3 Maintenance				
3.40	Is external woodwork painted or treated with decorative wood preservative?			
3.41	Are doors and windows of a standard design?			
3.42	Are anchor points specified for window cleaning/fixing ladders?			
3.43	Are inspection hatches to pipes and cables included?			
3.44	Are pipes colour coded with paint?			
3.45	Are plastic waste disposal systems specified?			
3.46	Are the quality and type of floor coverings conducive to easy maintenance?			
3.47	Have pitched roofs been specified?			
3.48	Can the number of edges to grass areas be reduced?			
3.4 Furniture and Equipment				
3.49	<p>Is it necessary?</p> <ul style="list-style-type: none"> • what is the need to be met? • have alternatives been considered? • what are they? • has specialist advice from elsewhere in the organisation been sought? • if technological change is occurring, should items be hired rather than bought? • will changed circumstances make it obsolete in the near future? 			
3.50	<p>How has the quality been determined?</p> <ul style="list-style-type: none"> • will it fit in the room? • how does it compare to recognised guidelines? • ration of occupants or group size to quantity? • is it the same as existing? • is it the same as elsewhere in the organisation? • are capacities of related items compatible? 			
3.51	<p>How has the quality been determined?</p> <ul style="list-style-type: none"> • is it the same as existing? • is it the same as elsewhere in the organisation? • are higher qualities demanded for status? 			

3.5 Miscellaneous				
3.52 Is there any evidence of extravagance in the design or specification? For example: <ul style="list-style-type: none"> • a toilet for each senior employee; • carpet up to the walls; • unconventional edging to roads; • hand-made furniture? 				
3.53 Are there any features of the design which will increase staffing requirements? For example: <ul style="list-style-type: none"> • many small rooms to clean instead of fewer large ones? 				
3.54 What kind of telephone system is proposed? <ul style="list-style-type: none"> • manual or semi-automatic? • how many extensions are planned? • what type are they? 				
3.55 What involvement of specialist purchasing officers will there be in obtaining nominated supplies?				
3.56 Will insurance costs be excessive?				
3.57 Are there any features of the design which will make the building difficult to demolish?				

Subject to the satisfactory resolution of any major points noted in the audit report, in my opinion we have met the overall audit objectives.

Signed

Date



*“Pacific Auditors Working
Together”*