COMPLIANCE AUDIT
ISSAI IMPLEMENTATION HANDBOOK

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VERSION 1, JANUARY 2022

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ACRONYMS & ABBREVIATIONS

AWP	Audit Working Paper
CA	compliance audit
GPG	Global Public Good
IDI	INTOSAI Development Initiative
IFPP	INTOSAI Framework of Professional Pronouncements
INCOSAI	International Congress of Supreme Audit Institutions
INTOSAI	International Organization of Supreme Audit Institutions
ISSAI	International Standards of Supreme Audit Institutions
QA	quality assurance
RMNC	risk of material non-compliance
SAI	Supreme Audit Institution
SoAQM	System of Audit Quality Management

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QUALITY STATEMENT FOR COMPLIANCE AUDIT ISSAI IMPLEMENTATION HANDBOOK VERSION 1 (JANUARY 2022)

The INTOSAI Goal Chairs' and IDI's joint paper, Quality Assuring INTOSAI Public Goods that Are Developed and Published Outside Due Process, identifies three levels of quality assurance, as follows:

QUALITY ASSURING INTOSAI PUBLIC GOODS THAT ARE DEVELOPED AND PUBLISHED OUTSIDE DUE PROCESS – Levels of Quality Assurance

→ **Level 1:** Products that have been subjected to quality assurance processes equivalent to INTOSAI due process, including an extended period of transparent public exposure (90 days)

→ **Level 2:** Products that have been subjected to more limited quality assurance processes involving stakeholders from outside the body or working group responsible for the products' initial development. Quality assurance processes might, for example, include piloting, testing and inviting comments from key stakeholders, although not go as far as full 90-day public exposure.

→ **Level 3:** Products that have been subjected to rigorous quality control measures within the body or working group responsible for their development

Different levels of quality assurance may be appropriate for different Global Public Goods (GPG). This GPG has been developed according to quality assurance level 1.

Quality Assurance Protocol: Version 2.0

IDI's Protocol for Quality Assurance (QA) of IDI's Global Public Goods defines measures to ensure quality across the three levels of quality assurance outlined above. For quality assurance level 1, these measures include:

- approval by the IDI Board to create the GPG;
- formation of a competent product development team;
- peer review by experts external to the development team;
- modification based on review;
- proofreading, editing and translation of the document by competent persons;
- public exposure for a period of 90 days and consultation with relevant stakeholders representing views from most regions, most models of auditing, developed and developing countries, and from the perspective of global bodies;
- modifications of the document based on comments received during public exposure; and
- due approvals for the GPG version 1.

Updates to this GPG

To ensure this GPG remains relevant, IDI will undertake a major revision of this Compliance Audit ISSAI Implementation Handbook whenever there are changes in compliance audit ISSAIs. Major revisions will follow IDI's Protocol for Quality Assurance. In addition, light-touch reviews may be undertaken as needed. Such light-touch reviews will not usually be subject to this Protocol.

This GPG is owned by IDI's Professional SAIs work stream, which is responsible for the maintenance of this GPG.

Quality Assurance Review Process

Shourjo Chatterjee (Strategic Support Unit, IDI) has undertaken a QA review of the process followed for the development of this GPG, against QA Protocol Version 2.0. The QA reviewer is familiar with IDI's QA protocol for GPGs and was not involved in the development of the GPG. This QA review process is designed to provide all stakeholders with assurance that the IDI has carried out the quality control measures stated above, designed to meet quality assurance level 1.

Results of the Quality Assurance Review

The QA review of the process followed in developing this GPG concluded that the Protocol has been followed as required for quality assurance level 1 in all respects.

Conclusion

Based on the QA review, IDI assures the users of this GPG that this document has been subjected to a quality assurance process equivalent to due process for the INTOSAI Framework of Professional Pronouncements (IFPP), including an extended period of transparent public exposure.
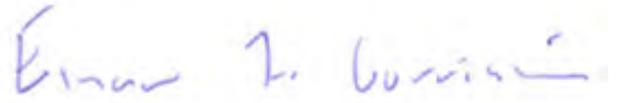
Einar Gørrissen
Director General
INTOSAI Development Initiative
January, 2022

Note: The Compliance Audit ISSAI Implementation Handbook, Version 1, has reached its designated expiry date and has accordingly undergone a light-touch review, undertaken in line with the IDI Quality Management System policy and guidance (pp. 12–13), to confirm its continued relevance. The review was led by Shofiqul Islam, Senior Manager and approved by Karma Tenzin, Assistant Director General. The light touch review identified minor updates including an update on Quality Management chapter that reflects the requirements of ISSAI 140 — Quality Management for Supreme Audit Institutions (SAIs) and its linkage to quality management at the compliance audit engagement level. The Handbook has been reissued with a revised publication date of January 2026.

ABOUT THE HANDBOOK

BACKGROUND

The IDI developed the first compliance audit (CA) ISSAI[1] Implementation Handbook in 2014, under the ISSAI Implementation Initiative (3i Programme). At that time, the Handbook was based on the old level-4 compliance audit ISSAIs (ISSAI 4100 and 4200) and the level-3 ISSAIs (ISSAI 400 and ISSAI 100). These standards provided the basis of the audit methodology described in the first compliance audit handbook.

INTOSAI approved the new ISSAI 4000 - Compliance Audit Standard[2] at the 2016 INCOSAI. As the authoritative standard for compliance audits, ISSAI 4000 has undergone significant changes from the earlier versions of the CA ISSAIs. Subsequently, to reflect changes in the ISSAIs, the IDI initiated revision of the CA ISSAI Implementation Handbook and developed it as a Global Public Good (GPG). The GPGs are products and tools created by the IDI to contribute to global knowledge creation, capacity development, and enhanced performance of SAIs.

PURPOSE OF THE HANDBOOK

The purpose of this Handbook is to provide practical guidance, assist SAIs and their auditors in conducting ISSAI 4000 compliant compliance audits. The Handbook incorporates an ISSAI 4000-based audit methodology, including explanations of the audit process and suggested audit working paper templates.

PROCESS OF DEVELOPING THE HANDBOOK

The IDI followed its Protocol for Quality Assurance of its Global Public Goods V2.0[3] for the development of this Handbook. Section 6 of the protocol, Conversion of existing products into a Global Public Good,

determines the due process for ensuring the quality of this version of the Handbook. The process first requires developing Version 0 of the Handbook and exposing it for comments. Based on the comments and feedback received, Version 0 is then updated and termed as Version 1 of the Handbook.

A product development team from the SAIs of different INTOSAI regions and the IDI staff developed the first draft of this Handbook. A group of compliance audit experts independently reviewed the draft Version 0 of the Handbook. After that, Version 0 was finalised, and the IDI placed it on its website for public exposure for 90 days.

During exposure, the IDI informed the relevant stakeholders about the availability of Version 0 on the IDI website and requested their feedback and comments on the Handbook. The stakeholders included, among others, the SAIs, ISSAI facilitators, and auditors engaged in IDI's ISSAI implementation initiative. Stakeholders also covered were the INTOSAI General Secretariat, INTOSAI regions, INTOSAI Professional Standards Committee, members of the INTOSAI Compliance Audit Subcommittee, INTOSAI Knowledge Sharing Committee, IDI's resource persons and experts, and the donor community.

At the same time, the IDI translated Version 0 of the Handbook into Spanish, Arabic and French and placed it on the IDI website for exposure. The IDI sent the Handbook to the OLACEFS (Organisation of Latin American and Caribbean Supreme Audit Institutions), ARABOSAI (Arab Organisation of Supreme Audit Institutions) and CREFIAF (Le Conseil Régional de Formation des Institutions Supérieures de Contrôle des Finances Publiques de l'Afrique Francophone sub-Saharienne) regional secretariats to disseminate among the SAIs of these regions for comments.

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[1] ISSAI - The International Standards of Supreme Audit Institutions (ISSAI). The complete and updated collection of professional standards and best practice guidelines for public sector auditors.

[2] ISSAI-4000-Compliance-Audit-Standard.pdf

[3] http://www.idi.no/en/idi-library/global-public-goods

The IDI acknowledges the valuable comments it has received from stakeholders regarding the Version 0 exposure. These comments were duly incorporated, helping immensely to improve the Handbook and to develop Version 1. As Version 1 of the Handbook now replaces Version 0, the IDI withdraws Version 0 on the date Version 1 becomes available.

The Department of Professional & Relevant SAIs of the INTOSAI Development Initiative completed a light-touch revision of this document in 2025. This version reflects the light-touch revision.

CONTENT OF THE HANDBOOK

The Handbook has nine chapters divided into four parts. Part A covers the basics of compliance auditing and explains its fundamental concepts as defined by the ISSAIs. Part B is for SAI management, which provides guidance on managing the compliance audit at the SAI level.

Part C is about conducting the compliance audit and describes the audit methodology covering the planning, gathering and evaluating evidence, and reporting phases. Part C also includes the relevant working paper templates (as exhibits at the end of this Handbook), which are designed to support the audit process and facilitate the application of the ISSAIs in practice. SAIs may need to modify the working paper templates to be consistent with their mandate, existing documentation, and audit practices. Part D explains the documentation and quality management processes of a compliance audit.

WHO CAN USE THIS HANDBOOK?

This Handbook would be most useful for SAI auditors and SAIs that have adopted ISSAI 4000 as authoritative auditing standards, or those that plan to adopt ISSAI 4000 as authoritative auditing standards for conducting compliance audits. This Handbook is not an authoritative document. We recommend that SAIs adapt the methodology outlined in this Handbook, taking into account their mandate and reporting requirements. The SAIs would also need to customise it to suit their audit practice, consistent with the context and environment in which the SAI operates.

HOW CAN AN SAI USE AND BENEFIT FROM THIS HANDBOOK?

SAIs can use this Handbook in full or in parts, as required by the SAI, that cover different aspects of compliance audit practice. Generally, the SAIs are at varying levels of development in their compliance audit practices, both in their organisational requirements for audits and in their audit practices. SAIs can use this Handbook to address the identified areas of need for becoming ISSAI compliant.

Part B explains the SAI's organisational requirements (as per ISSAI 4000) for conducting a compliance audit. The SAI management and staff responsible for methodology may analyse this part and determine the necessary measures the SAI needs to take to satisfy the organisational requirements of ISSAI 4000. The organisational requirements regarding documentation are further elaborated in Part D to assist the SAI in conducting ISSAI-compliant audits.

SAIs that have a compliance audit methodology and aim to conduct the audit following the ISSAI 4000-based methodology may wish to consider Part C, along with Parts B and D. Part C will assist the SAI to analyse how the SAI's existing compliance audit practice corresponds to the ISSAI 4000-based methodology as suggested in the Handbook. Through this analysis, the SAI can determine at which points in the audit process its methodology is deficient in the aspects required by ISSAI 4000, as described in the Handbook.

SAIs can use the ISSAI Compliance Assessment Tool for compliance audit (CA iCAT)[4] to identify the gaps between the SAI's CA audit practice and the requirements of ISSAI 4000. The iCAT results will highlight the areas the SAI needs to address to make the audit practice ISSAI-compliant.

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[4] CA iCAT tool (Version 1) is available on the IDI website: Compliance Audit iCAT V1 (idi.no)

PART A
COMPLIANCE AUDIT BASICS

VALUE AND BENEFITS OF COMPLIANCE AUDITS

1.1 What are the value and benefits of compliance audits?

1.2 What are the key enablers in delivering value through compliance audits?

1.3 High-quality compliance audits and IFPP

This chapter reflects on compliance audits within the broader framework of SAI audits, the ISSAIs, and the value they add. The chapter highlights the different ways an SAI can adopt the ISSAIs for compliance audits and when the SAI can refer to them in its compliance audit reports. Going beyond the requirements of the standards, the chapter also reflects on the impact of compliance audits, the mainstreaming of gender and inclusiveness considerations, and the agility of compliance audits to respond to emerging issues.

1.1 WHAT ARE THE VALUE AND BENEFITS OF COMPLIANCE AUDITS?

Supreme Audit Institutions contribute value and benefits for all by exercising independent external oversight to ensure accountability, transparency, inclusiveness, ethical behaviour and effectiveness of public governance. SAIs provide assurance on the financial statements of governments and government bodies, examine compliance with applicable laws and regulations, and offer recommendations to enhance the economy, efficiency and effectiveness of service delivery, governance or outcomes that impact people and the planet.

The auditing of government and public sector entities by SAIs has a positive impact on trust in society because it focuses the minds of the custodians of public resources on how well they use those resources. Such awareness supports desirable values and underpins accountability mechanisms, which, in turn, lead to improved decisions. Once SAI's audit results are made public, citizens can hold the custodians of public resources accountable. In this way, SAIs promote the efficiency, accountability, effectiveness, transparency, and inclusiveness of public institutions.

Public-sector auditing is essential because it provides legislative and oversight bodies, those charged with governance, and the general public with information and independent, objective assessments of the performance of government policies, programmes or operations. Public sector auditing is a systematic process of objectively obtaining and evaluating evidence to determine whether information or actual conditions conform to established criteria.[5]

While SAI mandates and legal frameworks are quite diverse across the INTOSAI community, ISSAI 100 recognises three types of audits usually carried out by SAIs: financial audit, compliance audit and performance audit. The three audit types are different, considering that each type has its own focus area and audit approach.

The financial audit focuses on determining whether an entity's financial information is presented in accordance with the applicable financial reporting and regulatory framework. This is accomplished by obtaining sufficient and appropriate audit evidence to enable the auditor to express an opinion as to whether the financial information is free from material misstatement due to fraud or error[6].

A performance audit is an independent, objective and reliable examination of whether the government undertakings, systems, operations, programmes, activities or organisations are operating in accordance with the principles of economy, efficiency and effectiveness, and whether there is room for improvement[7].

A compliance audit is an independent assessment of whether a given subject matter complies with applicable authorities identified as criteria. This is done by assessing whether activities, financial transactions and information comply, in all material respects, with the authorities that govern the audited entity[8].

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[5] ISSAI 100.18

[6] ISSAI 100.22

[7] ISSAI 300.9

[8] ISSAI 400.12

Achieving value and benefits through compliance audits is a complex process. It requires several actors across different functions to work together in a coherent and coordinated manner. These actors include both state and non-state actors, as shown in Figure 1.1. In order to contribute and deliver value, compliance auditors need to scan the ecosystem in which they operate and identify the actors and processes that need to be engaged with throughout the audit.

Compliance audits can add value in many different ways, through their coverage; high-quality audit reports in the public domain; and recommendations leading to more transparent, accountable, and inclusive compliance frameworks, decision-making, and greater compliance with applicable authorities by those charged with governance.

FIGURE 1.1
Value and benefits for all

National, State/Provincial and Local level legislative bodies, constitutional bodies and Judiciary, oversight bodies

State Actors

International & Regional Actors

National, State/Provincial and Local level ministries, departments, offices, programmes, projects, state owned bodies, internal oversight bodies

International/ Multilateral Bodies, Regional Bodies, CSOs, Professional Bodies

Value & Benefits for All

Executive State Actors

Non State Actors

People, CSOs, Media, Academia, Professional Bodies, Private Sector

Compliance audits promote transparency

Transparency can be defined as the fundamental, commonly agreed-upon principle of disclosure that makes policies, legal and institutional frameworks, and information related to decisions available to the public in a comprehensible, accessible and timely manner. Through compliance audits, SAIs can ascertain if audited entities comply with transparency requirements. While publication of an SAI's compliance audit reports leads to greater transparency, executive action on the recommendations made by the SAI leads to more transparent compliance systems in the long run.

Compliance audits help the citizens hold to account those charged with governance and improve accountability mechanisms in the public sector

Accountability is about the relationship between the State and its citizens, and the extent to which the State is answerable for its actions. The concept of accountability refers to the legal and reporting frameworks, organisational structure, strategy, procedures and actions that ensure every organisation that uses public money and makes decisions affecting people's lives is held responsible for its actions. The principles and concepts necessary to public sector accountability include transparency, fairness, integrity and trust. Compliance audits can ensure accountability by serving as a deterrent through adequate and regular oversight of compliance with authorities. Compliance audit reports can help citizens hold those charged with governance to account. Action on compliance audit conclusions and recommendations will lead to more accountable systems and actions by governments in the future.

Compliance audits promote inclusiveness

Besides contributing to transparency and accountability, compliance audits can also promote inclusiveness. Compliance auditors can verify if the authorities, rules, and regulations that provide for **inclusion** across different areas are complied with by those charged with governance. For example, compliance auditors can assess whether socio-economic schemes for beneficiaries from vulnerable groups are implemented in accordance with requirements and whether the beneficiaries are genuine. Compliance audits can also comment on the extent to which inclusion considerations are incorporated into government compliance frameworks.

Compliance audits contribute to ethical behaviour

Behaving ethically in all situations is a fundamental value for everyone, especially those charged with governance. Compliance audits help promote ethical behaviour in the public sector by providing oversight of the extent to which decisions are made in accordance with the requirements of applicable codes of ethics and by making recommendations for improving compliance frameworks for ethics.

Compliance audits contribute to the fight against fraud and corruption

Compliance audits have both preventive and detection value in case of fraud and corruption in public institutions. SAIs can build red flags, assess the vulnerability of compliance systems and test actual compliance to detect instances of fraud and corruption. Depending on their mandates and capacities, SAIs can work together with anti-corruption agencies, hand over their findings to other authorities for further investigations or conduct such investigations themselves.

Compliance audits contribute to creating a culture of compliance

As mentioned earlier, adequate compliance audit coverage, high-quality compliance audits and follow-up and executive action on instances of non-compliance can, in the long run, contribute to greater awareness of the importance of compliance, act as a deterrent for non-compliance and facilitate a more compliant culture in government institutions.

By examining transparency, accountability, inclusiveness and ethical behaviour across sectors – public health, education, infrastructure, technology, environment and so on – compliance audits contribute to value and benefits for both people and planet.

We can also examine the value and benefits of compliance audits from the perspective of a value chain of outputs, outcomes and contribution to impact. Illustration 1.1 below shows this.

This value chain, leading to value and benefits for all, works on certain assumptions: enabling SAI independence and mandate, adequate SAI resources and capacities, robust audit methodology, supportive stakeholders, SAI's ability to follow up and audited entities that take action on SAI recommendations. The delivery of value is compromised if any link in the chain or any assumption doesn't work. This value chain is further affected by the country's political, social, economic and cultural environment.

ILLUSTRATION 1.1:
Compliance audit value chain

- Adequate audit coverage
- Timely, high-quality compliance reports in the public domain
- Actionable recommendations for greater compliance

- Transparency, accountability, ethical behaviour and inclusion in public institutions
- A culture of compliance in public sector
- Enhanced trust among citizens in public institutions

COMPLIANCE AUDIT OUTPUTS

COMPLIANCE AUDIT OUTCOMES

CONTRIBUTION TO IMPACT

- Increased compliance with applicable authorities, rules and regulations
- More robust compliance frameworks put in place to ensure future compliance

1.2 WHAT ARE THE KEY ENABLERS IN DELIVERING VALUE THROUGH COMPLIANCE AUDITS?

This section reflects on key enablers for delivering value or contributing to impact through compliance audits.

1. **Enabling SAI mandate and legal framework:** The SAI needs an enabling mandate and independence to be able to determine the compliance audits it will take up, decide on the methodology, issue and publish its report, and follow up on action taken.

2. **SAI leadership**: SAI leaders play a key role in strategising to deliver value, mobilising resources, making decisions and, most importantly, setting the tone and a culture that focuses on delivering value.

3. **High-quality audits:** The SAI needs a credible and high-quality product to add value. As such, compliance with applicable standards and the SAI's ability to demonstrate it through robust quality systems are crucial.

4. **Impact-driven compliance audits:** If the compliance audits are to contribute to impact, the SAI needs to have processes and practices that mainstream impact considerations throughout the audit process. This includes planning for impact and focusing on impact while conducting and reporting on the audit. Ensuring timely reports that reach a wide set of stakeholders is also key.

5. **Stakeholder engagement throughout the audit process:** SAIs cannot deliver value alone. It takes a coalition of stakeholders and an entire ecosystem of actors working together to deliver the impact and value of compliance audits. Keeping this in mind, it is important for the SAI to determine key stakeholders and their level of engagement at the outset of the audit process. This can be done strategically for the compliance audit practice as a whole and for individual compliance audits.

6. **Robust follow-up of compliance audits:** The auditor's role does not end with the issuance of the report. Suppose the compliance audits conducted by the SAI are to deliver value. In that case, the SAI needs a robust follow-up mechanism that clarifies the expected corrective action, follows up with those responsible, and monitors and measures the actions taken on compliance audit conclusions and recommendations.

7. **Agile and flexible compliance audits:** Given the pace at which things move in these times, SAIs need to build agile features into their compliance audit practice. Please refer to chapter 4 of IDI's practical guide on Audit of Transparency, Accountability and Inclusiveness (TAI audits) of the use of emergency funding for COVID-19 to learn more about an agile approach to compliance audits (TAI Guide (www.idi.no)).

8. **Focus on gender and inclusiveness considerations:** As it is the vulnerable and marginalised sections of the population that are most adversely affected by non-compliance and the lack of integrity and corruption in public institutions, we believe that it is important for SAIs to reflect on gender and inclusiveness considerations in their compliance audit practice. SAIs can do this by mainstreaming such considerations in compliance audits across sectors and/or focusing on specific areas of marginalisation and vulnerability as the subject matter of compliance audits, e.g., audits of socio-economic packages during COVID-19 for single mothers. Please refer to the TAI Audit Question Bank (TAI Audit Question Bank (idi.no)) for examples of inclusiveness questions that can be asked in compliance audits.

1.3 HIGH-QUALITY COMPLIANCE AUDITS AND IFPP

In the previous section, we discussed how high-quality compliance audits are essential to delivering value and benefits. In this section, we explore the link between high-quality compliance audits and the INTOSAI Framework of Professional Pronouncements (IFPP). As part of this exploration, we will also discuss what it means for an SAI to adopt compliance audit standards, the different ways of referring to the ISSAIs, and the implementation of an ISSAI-compliant compliance audit practice.

The IFPP consists of INTOSAI Principles (INTOSAI-P), International Standards of Supreme Audit Institutions (ISSAI) and INTOSAI Guidance (GUID):

CATEGORY NUMBER	CATEGORY	CLASSIFICATION CRITERIA
INTOSAI P1-9	INTOSAI founding principles	Founding historical principles specifying the role and functions that SAIs should aspire to. These principles may be informative to Governments and Parliaments, as well as SAIs and the wider public and maybe used as reference in establishing national mandates for SAIs.
INTOSAI P10-99	INTOSAI core principles	Core principles that support the founding principles for an SAI, clarifying issues in relation to the SAI's role in society as well as high level aspirations for the proper functioning and professional conduct of an SAI.
ISSAI 100-129	Fundamental principles of public sector auditing	Defines basic set of concepts and principles that defines public sector auditing and the different types of engagements supported by the ISSALs.
ISSAI 130-199	SAI organizational requirements (SAI level)	Requirements for organizational functions of an SAI that are designed to enhance the performance of quality audits.
ISSAI 200-299	Financial audit principles	These define the elements and principles of financial auditing, with reference to the fundamental principles of public sector auditing
ISSAI 300-399	Performance audit principles	These define the elements and principles of performance auditing, with reference to the fundamental principles of public sector auditing.
ISSAI 400-499	Compliance audit principles	These define the elements and principles of compliance auditing, with reference to the fundamental principles of public sector auditing.
ISSAI 2000-2899	Financial audit standards	Standards for financial auditing, in conformity with the financial audit principles.
ISSAI 3000-3899	Performance audit standards	Standards for performance auditing, in conformity with the performance audit principles.
ISSAI 4000-4899	Compliance audit standards	Standards for compliance auditing, in conformity with the compliance audit principles
GUID 1900-1999	SAI organisational guidance	Guidance that supports the SAI in enhancing organisational performance in practice related to the organizational requirements and ISSAI implementation.
GUID 2900-2999	Supplementary financial audit guidance	Guidance that supports the auditor in the financial audit process on how to apply the ISSAIs in practice.
GUID 3900-3999	Supplementary performance audit guidance	Guidance that supports the auditor in the performance audit process on how to apply the ISSAIs in practice.
GUID 4900-4999	Supplementary compliance audit guidance	Guidance that supports the auditor in the compliance audit process on how to apply the ISSAIs in practice.
GUID 5000-5999	Subject matter specific guidance	Guidance that supports the auditor in understanding a specific subject matter and the application of the relevant ISSAIs.
GUID 9000-9999	Other guidance	Other guidance that supports the auditor.

Reserved for future development based on ISSAI 100

ISSAI 600-699	Principles for other engagements	These define the elements and principles of other engagements, with reference to the fundamental principles of public sector auditing.
ISSAI 6000-6499	Standards for other engagements	Standards for other engagements in conformity with the fundamental principles of public sector auditing. This may include other INTOSAI audit types or standards developed by other recognized standard setters and adopted by INTOSAI.
GUID 6500-6999	Supplementary guidance on other engagements	Guidance that supports the auditor in other engagements on how to apply the ISSAIs in practice.
7000-8999		Available for any future needs.

Moving towards high-quality compliance audits through full compliance with ISSAIs

An SAI's journey towards high-quality compliance audit practice has the following key elements (as illustrated in Illustration 1.2):

Adoption of compliance audit ISSAIs

Adoption of compliance audit ISSAIs refers to the decision-making process within the SAI, whereby it decides on how it will refer to the ISSAIs in its compliance audit practice. As explained in ISSAI 100:8, the SAIs can adopt the ISSAIs in different ways.

The Fundamental Principles of Compliance Auditing (ISSAI 400) provide the SAIs with a basis for the adoption or development of standards and guidelines for compliance auditing.

The principles in ISSAI 400 can be used in three ways:

- As a basis for the adoption of the compliance audit standards (ISSAI 4000) as the authoritative standards
- As a basis on which SAIs can develop their auditing standards
- As a basis for the adoption of consistent national standards

As a basis for the adoption of ISSAI 4000 as the authoritative compliance audit standards: SAIs could consider directly adopting the ISSAI 4000, the compliance audit standards, as their authoritative compliance auditing standards. As the ISSAI 4000 has been developed to reflect best practices, the SAIs are encouraged to strive towards adopting them in full as their authoritative standards. In some environments, this might not be possible due to the absence of basic administrative structures or because laws or regulations do not provide the premises for carrying out audits following the ISSAI 4000. In such cases, SAIs may develop standards, based on or adopting national standards consistent with the Fundamental Principles of Compliance Auditing – ISSAI 400[9].

As a basis on which SAIs can develop their own standards: Some SAIs may be conducting compliance audits as per their mandate, but they may not have any governing auditing framework to support their work. These SAIs can develop their compliance audit standards in line with the fundamental principles of compliance auditing of ISSAI 400. The ISSAIs emphasise the need for SAIs to review their mandates, laws, and regulations when adopting them. Thus, these principles do not override the existing mandates, rules and regulations that govern the SAI audit practices. [10]

As a basis for the adoption of consistent national standards: Some SAIs may already have their national standards for conducting compliance audits. ISSAI 400 provides a framework for these SAIs as the fundamental principle. SAIs can analyse their existing practices and standards vis-à-vis the ISSAIs, identify gaps and modify their governing auditing standards to ensure alignment with the principles of ISSAI 400.

ILLUSTRATION 1.2:
Journey towards high-quality compliance audit

Adoption of compliance audit ISSAIs

Implementation of compliance audit practice as per standards

Independent assurance of quality of compliance audits through robust quality mechanisms

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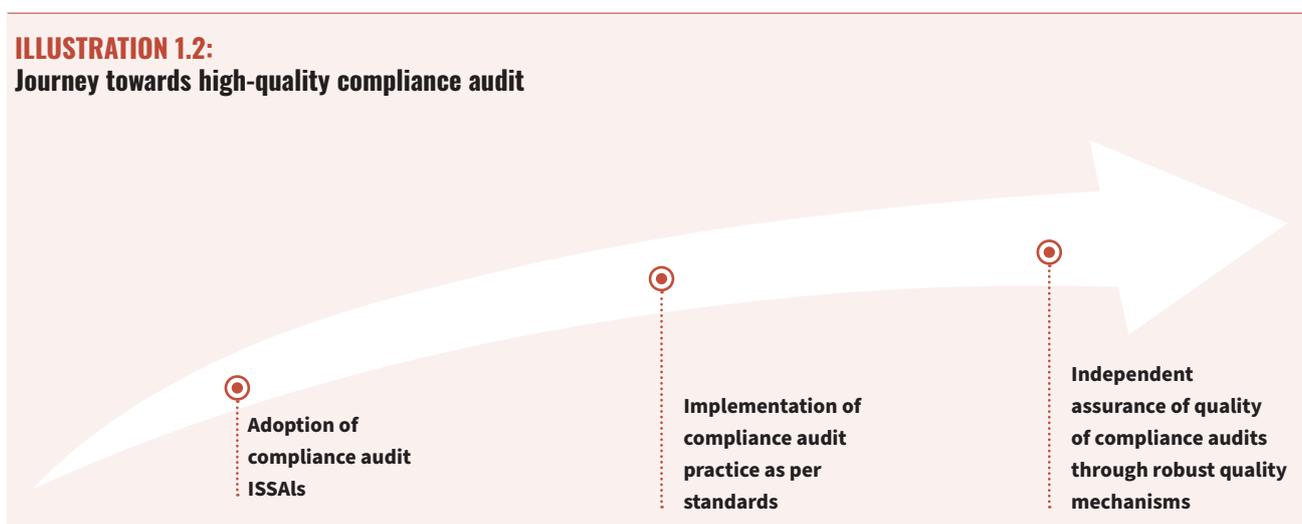
[9] ISSAI 400.7

[10] ISSAI 400.7

Implementation of compliance audit practice as per standards

After deciding on adoption, the SAI would need to put in place mechanisms for implementing a compliance audit practice that meets the requirements of the adopted standards. In order to do so, the SAI needs:

- A compliance audit methodology that is aligned to the standards: The methodology would define the compliance audit process and quality mechanisms.
- Competent compliance auditors: There needs to be an adequate number of compliance auditors who demonstrate the required competencies to carry out compliance audits and exercise professional judgment. Please refer to the Competency Framework for Public Sector Audit Professionals for more information on the competencies of a professional compliance auditor.
- Resources and supporting processes to carry out the compliance audits: This includes financial resources, infrastructure, support services, etc.

Ensuring audit quality of compliance audits

To ensure high-quality compliance audits, an SAI needs a System of Audit Quality Management (SoAQM) tailored to its context. Under revised ISSAI 140 — together with ISSAI 130 and 150 — establishing such a system is required when an SAI claims ISSAI compliance.

SoAQM changes quality management by focusing on system-level, risk-based measures that influence the entire audit practice. Rather than relying only on static manuals or procedures, it sets quality objectives and allows flexibility in how those objectives are achieved. Its risk-based approach helps the

SAI identify issues early and prioritise responses. Monitoring, remediation and evaluation processes enable timely correction of deficiencies and support continuous improvement.

System-level quality risk management, monitoring and evaluation drive quality at the engagement level. In addition, audit supervisors or directors may identify engagement-specific quality actions — for example, additional review steps, closer supervision, or a need for consultation — when specific risks apply only to a particular audit.

Making reference to the ISSAIs in an SAI's compliance audit report

SAIs should declare which standards they apply when conducting audits, and this declaration should be accessible to the users of the SAI's reports. SAIs are encouraged to make such statements a part of their audit reports[11]. The audit report users need to know how the SAIs conducted the audit and which methodology they followed. It is through this declaration that the users can have confidence in the information provided in the audit report. They recognise that ISSAIs require the SAI to plan and perform the audit to obtain reasonable assurance about whether the subject matter is or is not in compliance with the applicable authorities. The user also understands, through this declaration, that the audit includes, on a test basis, examining evidence supporting the findings and conclusions made in the audit. If the SAI does not make this declaration in its audit report, users will not know which process the SAI followed. Also, users will not be able to assess the quality of the audits conducted, which could affect the credibility of audit reports with stakeholders.

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[11] ISSAI 100.8

When the SAI complies with ISSAIs and refers to the ISSAIs in its compliance audit report, it has two options:

1. An SAI may fully comply with its national standards, which is consistent with the fundamental auditing principles: ISSAI 400 for a compliance audit. In such a case, the SAI can make reference in the compliance audit report by stating (ISSAI 400.8):

   'We conducted our audit in accordance with [country national standards], which are based on [or consistent with] the fundamental auditing principles for compliance audit ISSAI 400 of the International Standards of Supreme Audit Institutions.'

2. For a compliance audit, an SAI may fully comply with ISSAI 4000 - *Compliance Audit Standard.* In such a case, the SAI can make reference by stating (ISSAI 400.9):

   '… We conducted our [compliance] audit[s] in accordance with the International Standards of Supreme Audit Institutions [on compliance auditing].

ISSAI 4000.14 states that if all relevant requirements of ISSAI 4000 have not been fulfilled, a reference to ISSAI 4000 shall not be made without disclosure of that fact and further explanations about the consequences thereof. Compliance with ISSAI 4000 refers to an SAI's compliance with all relevant[12] requirements of ISSAI 4000 in an audit engagement or the SAI's overall compliance audit practice[13]. This implies that to refer to the ISSAIs in its audit report, the SAI must either have an ISSAI-compliant audit practice or a specific audit which is ISSAI-compliant.

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[12] SAIs can comply both within an individual compliance audit and across the compliance audit practice.

[13] Audit practice refers to a set of audits conducted under the same organisational arrangement that follows the same standards, methodology, competency requirements for audit teams, quality control and quality assurance arrangements.

GENERAL CONCEPTS OF THE COMPLIANCE AUDIT

2.1 The three parties of a compliance audit

2.2 Subject matter and subject matter information of compliance audit

2.3 Authorities and criteria in a compliance audit

2.4 Compliance audit as an assurance engagement

2.5 Different ways of conducting a compliance audit

2.6 Steps of a compliance audit

This chapter starts by explaining the three parties, the subject matter and the criteria of a compliance audit. It introduces the different approaches of conducting compliance audits and highlights the two types of engagement: direct reporting and attestation engagement. This chapter explains the levels of assurance that can be provided in the audit report – reasonable or limited. It explores the options available to an auditor when deciding on the appropriate type of compliance audit to conduct. The chapter concludes with an illustration of the compliance audit process.

2.1 THE THREE PARTIES OF A COMPLIANCE AUDIT

Compliance audits assess whether activities, transactions, and information comply, in all material respects, with the authorities that govern the audited entity[14]. The ISSAIs on compliance audits identify the three related parties involved in an audit and explain their relationships. ISSAI 400.35 states that 'compliance auditing is based on a three-party relationship in which **the auditor** aims to obtain sufficient appropriate audit evidence in order to make 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 a compliance audit:

- The **auditor** refers to the SAI.
- The **intended users** are the individuals, organisations or classes for whom the auditor prepares the audit report. In compliance auditing, the legislature, as the representative of the people, is the ultimate user of the audit reports. However, according to the standards, the users can also be oversight bodies, those charged with governance or the general public[15].
- 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 audit's subject matter[16].

FIGURE 2.1:
The three parties of the compliance audit
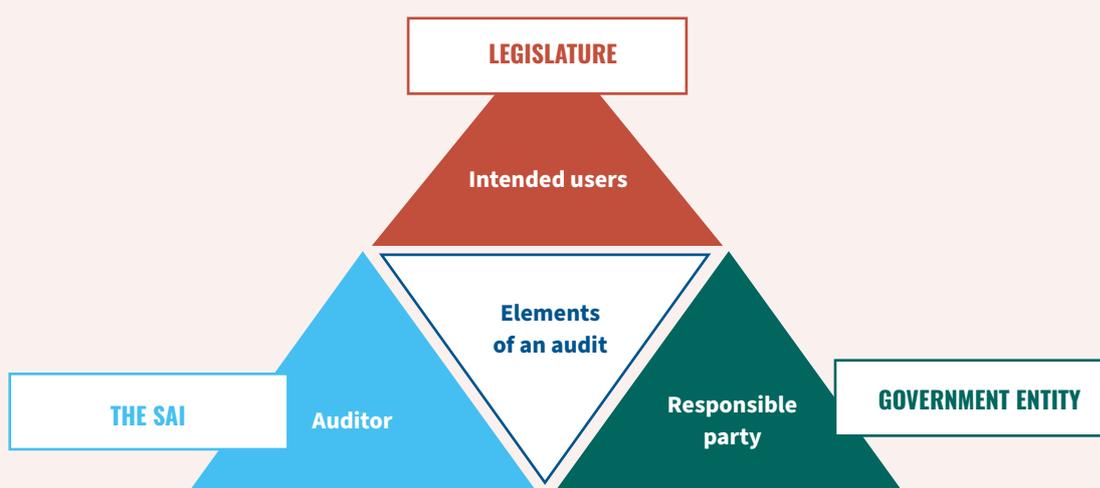
[14] ISSAI 400.12

[15] ISSAI 100.25

[16] ISSAI 400.37

It is essential to consider the relationship between the three parties; the responsibilities of each party, expectations from the other and how to meet those expectations. Although there are different models, usually the legislature empowers the government entities to perform specific duties by providing them with the budget and by establishing a legal framework to govern budget spending on different activities and services. The executive branch of government (e.g. the entities and public officials) is responsible for the management of public funds. The public officials' exercise of authority is subject to legislative **control**. But establishing this control depends on receiving timely and accurate information on how the entities are fulfilling their responsibilities. The legislature needs **information** about the entities and their activities for public policy decision-making purposes. The SAI is responsible for providing this information to the legislature. As such, the SAI should have a proper understanding of the needs and expectations of its intended users. The SAI has to be aware of the evolving environment in the government, the changing needs of information from the users and how it can provide the appropriate information to the users through its audit report.

2.2 SUBJECT MATTER AND SUBJECT MATTER INFORMATION OF COMPLIANCE AUDIT

The auditor's responsibility in compliance auditing includes determining whether the information related to a particular **subject matter**, in all material respects, is in compliance with the relevant criteria, such as applicable laws, regulations, directives, terms of contracts and agreements, among others.

The audit subject matter is decided based on the SAI's mandate, the relevant authorities and the audit scope. The content and scope of the subject matter can vary widely in a compliance audit.[17] For SAIs which have mandated requirements for compliance audits, the selection of the subject matter should be based on their mandated tasks. Where the SAI

has the discretion to select the coverage of compliance audits, it performs the procedures necessary to identify significant and relevant areas and/or areas with a potential risk of non-compliance. Based on the identified area, the auditor defines the audit's subject matter. The subject matter of a compliance audit can be an entity, activities, operations, financial transactions or information.

Once the subject matter is known, auditors can identify related **authorities** and criteria for the compliance audit. The objective of an audit is to provide the intended user(s) with information on whether the audited public entities and subject matters comply with laws, legislative acts or decisions, regulations, policies, established codes and agreed-upon terms. These form the relevant **authorities** governing the subject matter or the entity.[18]

Subject matter information refers to the outcome of evaluating or measuring the subject matter against the criteria. The subject matter and subject matter information in compliance audit is associated with the concepts of direct reporting engagement and attestation engagements (explained in section 2.5).

Identifying the subject matter of the compliance audit

For some SAIs, the respective law or audit mandate defines the audit subject matter. In other cases, the selection of the subject matter is a strategic choice operationalised in the SAI's annual plan based on risk assessment and professional judgment. Subject matter should be of such a nature that it enables the auditor to gather sufficient and appropriate audit evidence to support an audit conclusion or opinion on it with the necessary level of assurance. How the subject matter is selected has an impact on the audit approach when it comes to audit evidence and resources.[19]

For example, if the subject matter of a compliance audit is 'an entity' and the subject matter information could be taken as the 'accounts of the entity' without defining a more specific scope. But looking at the

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[17] ISSAI 100.28, ISSAI 400.33

[18] ISSAI 4000.23

[19] ISSAI 4000.43

definition, it is also possible to take the 'entity' as the subject matter, and the subject matter information could be the entity's activities and transactions and all authorities governing them. Providing a conclusion on such a broad audit scope would require more time and resources for the SAI.

For this reason, ISSAIs recognise the relationship between the subject matter and the scope of compliance audits to narrow the issue, and make it manageable to audit. When the auditors plan a compliance audit, they will usually start with a broad subject matter, such as the entity. Still, as they become more knowledgeable during the audit process, they may modify the subject matter and scope to a more focused audit, which will make the results more meaningful for the users.

The audit scope defines the subject matter and what the auditor is going to audit. The **scope** depends on the needs of the intended user(s), the decided level of assurance, the assessed risk, and the competence and resources (both human and financial) available in the SAI.[20]

In some countries, the subject matter of the compliance audit may be indicated in the relevant laws, while in others, it may be determined through risk assessment and professional judgment. In some SAIs, auditable entities might have been classified as high-, medium- or low-risk entities. These SAIs may choose to conduct compliance audits of high-risk entities annually, while medium- to low-risk entities will be audited once every two to three years.

For some subject matters, it may be relevant to include more than one responsible party, especially for subject matters where more than one entity is involved in the operation or execution of the budget. In those cases, the number of the intended user(s) may also increase.[21] SAIs should, by considering their circumstances and mandate, establish a process to systematically determine the subject matter for conducting a compliance audit in line with the ISSAIs.

The auditor may consider the following list of possible subject matters as a reference:

- Financial performance:
  — use of appropriated funds (budget execution)
  — use of grants and loans

- Procurement
- Revenue collection, e.g., taxes, customs, excises
- Expenditures
- Service delivery – medical, education, etc.
- Public complaints
- Heritage protection
- Propriety of auditee officials and decision-making
- Health and safety
- Environmental protection
- Internal control framework
- Payments of social benefits, pensions
- Physical characteristics, zoning density, and access to government buildings

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[20] ISSAI 4000.44

[21] ISSAI 4000.106

2.3 AUTHORITIES AND CRITERIA IN A COMPLIANCE AUDIT

Definition of authorities

Authorities are the most fundamental element of compliance auditing. 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. In general, authorities include rules, laws and regulations, budgetary resolutions, policies, established codes, agreed terms, and general principles governing sound public sector financial management and the conduct of public officials.[22]

The extent of the auditor's work to obtain a sufficient understanding of the legal and regulatory framework will depend on the nature and complexity of the laws and regulations. However, the auditor needs to understand the relevant provisions of the legislation to the audit task. In all cases, the audited entity remains responsible for ensuring compliance with applicable criteria.

Hierarchy of authorities

Because of the variety of possible authorities, they may have mutually conflicting provisions and be subject to differing interpretations. Also, subordinate authorities may not be consistent with the requirements or limits set out in the enabling legislation, and there may be gaps in the legislation. To assess compliance with authorities, the auditor needs to have sufficient knowledge of the structure and content of the authorities themselves.[23]

When the auditor identifies conflicting authorities, it is essential to consider the hierarchy of the authorities: the higher level of authority will prevail over the subordinate authorities. For example, suppose an operational procedure or activity of a subject matter or an entity has been defined in the law. In that case, the internal regulations of the subject matter or entity must be in line with this law. If they are not, auditors should point out the contradiction, and if their mandate allows, recommend a change in the subordinate authority. This could also be audit

evidence if following the internal regulation has caused a non-compliance with the higher authority.

Similarly, when auditors are in doubt about the correct interpretation of authority, they should review the law's background and context to understand its intent and premises before using the authority as the benchmark. When faced with such a situation, auditors may bring it to their superior's attention so they can take an appropriate course of action during the audit.

Criteria

Criteria are the benchmarks derived from authorities used to evaluate the subject matter. Criteria can be specific or more general and may be drawn from various sources, including laws, regulations, standards, sound principles and best practices.

In compliance audits, the criteria may differ significantly from one audit to another. The criteria should be included in the report itself, or the report may refer to the criteria if they are contained in an assertion from management or are otherwise available from a readily accessible and reliable source.

Whichever of these options is chosen, the auditor should identify the criteria in the compliance audit report so that the report users can understand the basis for the auditor's work and conclusions. Criteria should be made available to the intended users to enable them to understand how the subject matter has been evaluated or measured. Without the frame of reference provided by suitable criteria, any conclusion is open to individual interpretation and misunderstanding. The responsible party should be able to comment on the audit criteria before the commencement of the audit to make sure that the audit will achieve the desired effect. Communication with the responsible party can prevent the audit results from being ignored in the discussion on the criteria when the conclusions are reported.

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[22] ISSAI 400.28 and 29

[23] ISSAI 400.30

If criteria have not been defined by the authorities, it is essential to identify criteria that carry the qualities described in the ISSAIs. Criteria must be relevant, complete, reliable, neutral, understandable, useful, comparable, acceptable and available.[24]

Types of criteria

Compliance auditing may be concerned with regularity (adherence to formal criteria such as relevant laws, regulations and agreements) or with propriety (observance of the general principles governing sound financial management and the conduct of public officials) aspects of the subject matter. Criteria for regularity and propriety are different.

Regularity: Regularity criteria can be derived from rules and regulations, international treaties and other agreements and codes of conduct.[25] These criteria also derive from the constitution, statutory instruments, orders, governmental or ministerial directives, guidelines and agreed-upon terms and conditions.

Propriety: Depending on the SAI's mandate and the nature of laws and regulations in the public sector context, the audit scope may include aspects of propriety. Propriety is defined as 'observance of the general principles governing sound financial management and the conduct of public officials.'[26] The use of propriety as a basis for audit may be common practice in some SAIs, but others may lack the mandate to assess it. Some SAIs use this approach in 'management audits' conducted at the request of a legislative body.

Propriety criteria are either the generally accepted principles or national/international best practices when the country's legislative body has not ratified them. When the legislature approves it, the criteria become part of the regulations. In some cases, they may be uncodified, implicit, or based on overriding principles of law, which provide sufficient flexibility to the SAIs to adopt propriety criteria for an audit relevant to their context. However, compliance with

best practices may not be perceived as mandatory in some jurisdictions or may not be suitable according to the mandate of some SAIs.

The auditor may face difficulty envisioning the aspects of propriety in public financial management. Generally, there are elaborate provisions in the country's financial rules, public expenditure management rules, procurement rules or in other regulations and the strict codes of conduct for ethical behaviour.

The examples below, which are extracts from the discussion of the public accounts committee of a country, highlight the audit's propriety aspect:

> *'The auditors estimated that Mr… had authorised the charging to the Corporation of £xxxx of his private expenditure and a further £xxxx of private expenses for other members of staff. The Committee considers that Mr…'s conduct, while Chief Executive…, did not meet the standards expected of those entrusted with the use of public funds, notably in his handling of travel and personal expenditure.'[27]*

> *'The former Institute Director was able to draw up his own rules for handling grievances or complaints, even for complaints involving himself. As a result, some individuals had to use outside channels such as the press…This was an unacceptable way to deal with the legitimate concerns of staff about the management of the Institute and its governance. We consider it inappropriate that severance settlements should include increased benefits to reflect the personal circumstances of individuals.'*

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[24] ISSAI 4000.118

[25] ISSAI 4000.114

[26] ISSAI 400.13

[27] https://www.public-audit-forum.org.uk/wp-content/uploads/2015/04/Propriety-and-conduct-in-the-public-sector.pdf, page 13-14

'To avoid any question of impropriety, specific reasons should always be recorded whenever a contract is not awarded to a tenderer who submits the lowest bid and is judged capable of meeting the key performance criteria. This would also provide a basis for informing the other short-listed firms why their bids had been unsuccessful.'

'.. the catalogue of mismanagement at the College's Training Shop, including what seems a disregard for basic tenets of financial control, and exposure to potential conflicts of interest. For example, over £xxxx was paid for driving services provided by a son of the head of the Shop, but there was no evidence that the work was completed.'

Once the auditor identifies the suitable criteria for regularity or propriety, they are operationalised for the particular circumstances of each audit to be able to reach meaningful conclusions.[28] The quality of the auditor's opinion or conclusion in a compliance audit largely depends on how the auditor establishes and applies the audit criteria in the audit.

2.4 COMPLIANCE AUDIT AS AN ASSURANCE ENGAGEMENT

Public officials are responsible for running the government entities in compliance with the authorities governing the entity's activities and for achieving the level of performance expected of them. If, for some reason, the entity fails to comply with the authorities, the responsible officials are held accountable.

The auditor audits an issue or subject matter to provide the intended user with some level of confidence that the entity complies with the applicable authorities. For the auditor to conclude on the status compliance of the entity or subject matter, in all material respects, the auditor must have sufficient audit evidence to support that conclusion. When users (e.g., the legislature, such as the Parliament) need information about the operations of the responsible party (the entity), the users may request the SAI for an independent assessment of the actual conditions of the responsible party. The SAI then conducts an audit and provides an 'assurance' on the situation to the users.

As such, an audit conducted by the SAI is an assurance engagement. An assurance engagement compliance audit enhances the credibility of the information provided by the responsible party. The auditor can provide this assurance through opinions and conclusions which explicitly convey the level of confidence, or in other forms.[29] The auditor will check whether the information provided by government entities or actual conditions within these entities comply with the 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' that reduces the risk to the users when using the specific information and that helps them to make informed decisions.

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[28] ISSAI 4000.119

[29] ISSAI 100.32

In ISSAI 4000.19(b) this is referred to as '… to enhance the degree of confidence of the intended user(s).' So, assurance is linked to how the auditor can gather audit evidence and how much work s/he must perform to be sure of the conclusions. When the auditor provides a conclusion with reasonable assurance, the auditor must decide which audit techniques to use, combine them, and then be able to conclude that 'the information provided is, in all material respects, correct.'

The intended users wish to be confident about the reliability and relevance of the information they receive and use it as a basis for their policy decision-making. Audits, therefore, provide information based on sufficient and appropriate evidence, and for that, the auditors should perform procedures to reduce or manage the risk of reaching inappropriate conclusions.[30]

An auditor performs procedures to reduce or manage the risk of providing incorrect conclusions, recognising that due to the inherent limitations in all audits, no audit can ever provide absolute assurance on the condition of the subject matter. The auditor should transparently communicate this limitation. 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.[31]

Reasonable assurance and limited assurance engagement

ISSAI 4000.30 states that the compliance audit report can provide either **reasonable assurance** or **limited assurance** to the users. These two levels of engagement are different in using the types of criteria, sampling, evidence-gathering procedures and reporting formats.

The two levels of assurance in compliance auditing convey the message differently to the users. In a reasonable assurance engagement, the auditor expresses that, in the auditor's opinion, the subject matter is or is not in compliance, in all material respects, with the stated criteria. In a limited assurance engagement, it conveys that nothing has come to the auditor's attention to cause him/her to believe that the subject matter is not in compliance with the criteria.

The auditor uses the terms reasonable or limited because even if they are meticulous in their work, there is always a chance that they may not identify every instance of non-compliance, and therefore can make a wrong conclusion. It is not possible to provide absolute (100%) assurance. Levels of assurance will be examined further during planning the audit, since the decision to provide limited or reasonable assurance will have an impact on the audit design. Reasonable or limited assurance can be provided both for direct reporting and attestation engagements in compliance auditing.[32]

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[30] ISSAI 100.31

[31] ISSAI 400.40

[32] ISSAI 400.41

2.5 DIFFERENT WAYS OF CONDUCTING A COMPLIANCE AUDIT

There are two different types of compliance audit engagements: attestation engagements and direct reporting engagements.[33] Attestation engagements and direct reporting engagements differ based on who prepares and measures or evaluates the subject matter.

- In **attestation engagements,** the responsible party, i.e., the entity, 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. Attestation engagements can be both reasonable and limited assurance engagements.

- 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 auditor presents the outcome of measuring the subject matter against the criteria 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.[34] The auditor may also present the outcome in the form of an elaborate answer to specific audit questions.[35]

Each assurance engagement (reasonable or limited) is either an attestation engagement or a direct reporting engagement. The subject matter could be either set out in the SAI's mandate or selected by the SAI.[36] The difference between the two types of audit is linked to subject matter and subject matter information.

In attestation engagements, the auditor attests the subject matter information, which may be a statement of compliance under an established, standardised reporting framework.[37] Here, the audit criteria are implicitly given by the presentation of the subject matter information. In these cases, the auditor needs to identify relevant audit criteria to conclude the correctness of the criteria provided in the subject matter information by the responsible party.[38]

The example in Illustration 2.1 below illustrates a compliance audit case for two countries involving direct reporting and attestation engagement. Both countries have a similar responsible party as the entity, and the same subject matter and scope for audit, but they differ in the subject matter information.

Considering who prepares the subject-matter information influences audit decisions; in the two country scenarios below, this consideration will lead to either a direct reporting engagement or to an attestation engagement.

ILLUSTRATION 2.1:
Case scenario on compliance auditing

	Country X	Country Y
Responsible party	National Tax Office (NTO) of country X	National Tax Office (NTO) of country Y
The subject matter of the audit	Tax revenues of Value Added Tax (VAT)	Tax revenues of Value Added Tax (VAT)
Subject matter information	-	Financial information related to VAT revenues
Audit criteria	VAT law and other laws and regulations governing the collection of taxes	VAT law and other laws and regulations governing the collection of taxes
User	Parliament	Parliament

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[33] ISSAI 100.24

[34] ISSAI 100.29

[35] ISSAI 400.59

[36] ISSAI 4000.31

[37] ISSAI 100.30

[38] ISSAI 4000.113

The scenario of country X:

Direct reporting engagement
The National Tax Office (NTO) of country X does not publish reports on tax collection. The website provides some statistics, but these are usually outdated and not detailed. The NTO is part of the government budget system, and due to the financial management framework, it does not produce a separate set of financial statements. Due to the way accounts are prepared, it is not possible to isolate NTO's tax revenues from tax revenues from other sources. Recently, the Parliament of country X has been discussing a reform initiative to improve tax collection from VAT. SAI management decided to conduct an audit on the tax revenues of VAT and submit the findings to the legislature.

In the scenario above, no subject matter information has been made available by the NTO (responsible party), despite the need for this information. Therefore, the SAI, through its audit, decided to provide the information to the users. The audit will directly evaluate the tax revenues of VAT (subject matter) against the applicable criteria and will give a conclusion. Based on the evaluation of the subject matter by the auditor, the SAI prepares the audit report and submits it to Parliament.

This type of audit is called a **direct reporting engagement**. In a direct reporting engagement, the audit is conducted, by the auditor, who measures or evaluates the subject matter, rather than the subject matter information.

The scenario of country Y:

Attestation engagement
The National Tax Office (NTO) of country Y presented a report to the Parliament regarding tax collection. Subject matter information has been produced by the NTO (responsible party) and presented to the Parliament (users) in the form of a report. (This information could also be in the form 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 tax revenues of VAT.

Standards refer to producing subject matter information as 'evaluation of subject matter against criteria.' In the scenario, NTO has provided subject matter information (evaluation) in the form of a report. In the report, the officials of the responsible party are making explicit or implicit claims (assertions) that the information (evaluation) on the tax revenues of VAT (subject matter) is true and fair in light of the laws and regulations (criteria).

The auditor's role in this scenario is to attest to the assertion – in the form of a conclusion or opinion – on whether the claim made by the NTO (responsible party) about the evaluation it provided is correct or not; and whether the officials have indeed followed the laws and regulations as they have claimed (explicitly or implicitly). This conclusion enhances the confidence of the legislature about the report (subject matter information) it has received.

To appreciate the broad scope of the compliance audit, the auditor should understand the link between assurance levels and types of audit. The table in Illustration 2.2 illustrates how the auditor can accomplish these levels and types of audit in practice. Each compliance audit conducted by the SAI may fall into one of the four cells shown in the table.

ILLUSTRATION 2.2:
Combination of levels of assurance and types of engagement in compliance auditing

Assurance level	Engagement type	
	Direct reporting (DR)	Attestation engagement (AE)
Reasonable assurance (RA)	RA-DR	RA-AE
Limited assurance (LA)	LA-DR	LA-AE

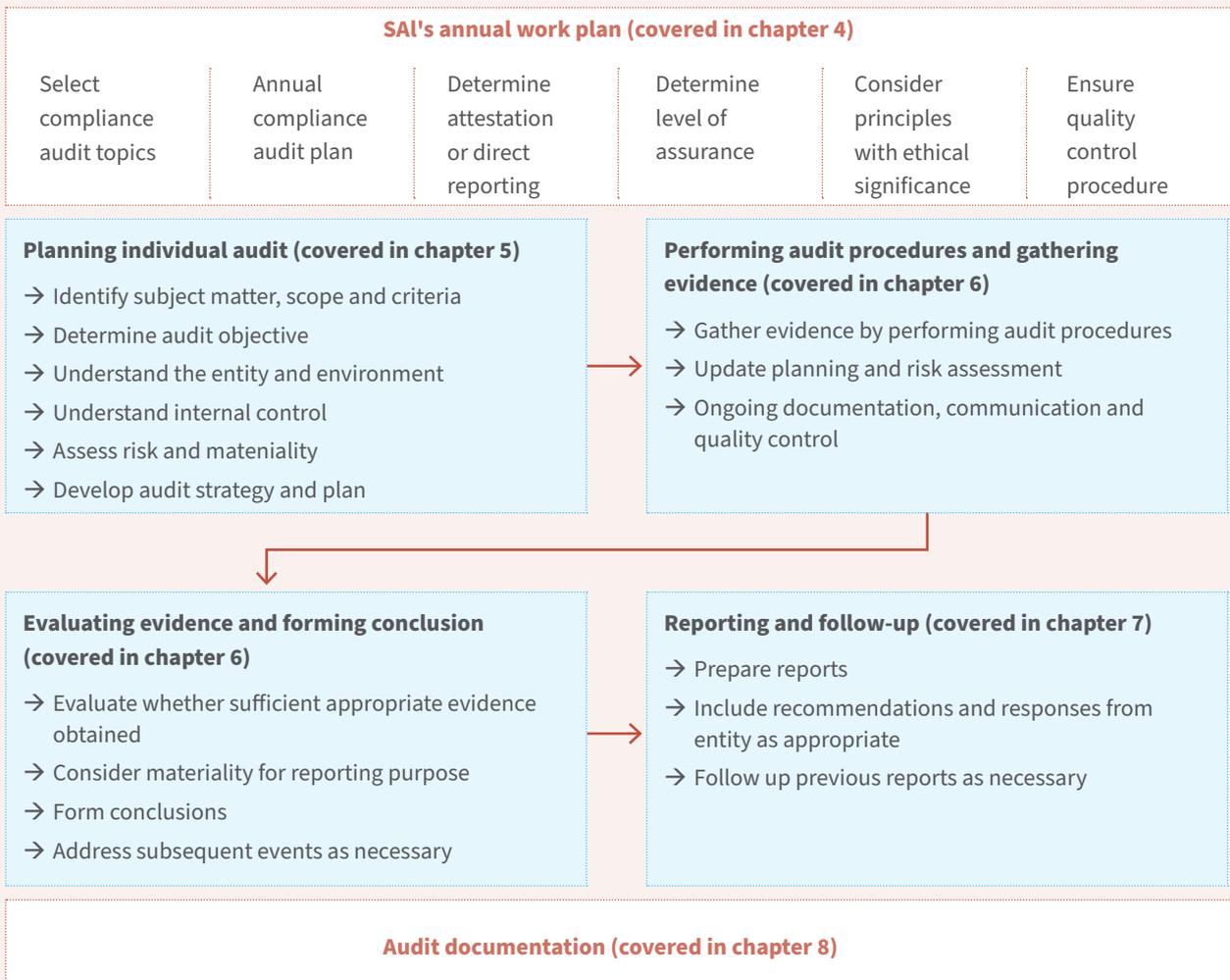**Compliance audit: Stand-alone or combined with other types of audits**

ISSAI 4000.15 states that compliance audits may be conducted either as a stand-alone engagement following ISSAI 4000 or combined with a financial or performance audit.[39] Different SAIs may use different approaches when carrying out compliance audits in combination with other types of audit. Compliance auditing is generally conducted as a separate compliance audit, in relation to the audit of financial statements or in combination with performance auditing.[40] The ISSAI 4000 does not provide detailed guidance on conducting combined audits.[41]

A stand-alone compliance audit engagement is performed separately, not in conjunction with financial auditing (which exists in some SAIs) or performance auditing. The ISSAIs state that compliance auditing conducted independently may be planned, performed and reported separately from an audit of financial statements and performance audits. It may be conducted regularly or on an ad hoc basis, as distinct and clearly defined audits, each related to a specific subject matter.[42] The ISSAI 4000 explains the process to be followed when SAIs conduct compliance audits as a stand-alone engagement. Accordingly, this Handbook explains the methodology for conducting a stand-alone compliance audit in accordance with ISSAI 4000.

2.6 STEPS OF A COMPLIANCE AUDIT

Illustration 2.3 below shows the compliance audit process.

ILLUSTRATION 2.3:
Steps of a compliance audit

SAI's annual work plan (covered in chapter 4)					
Select compliance audit topics	Annual compliance audit plan	Determine attestation or direct reporting	Determine level of assurance	Consider principles with ethical significance	Ensure quality control procedure

Planning individual audit (covered in chapter 5)
→ Identify subject matter, scope and criteria
→ Determine audit objective
→ Understand the entity and environment
→ Understand internal control
→ Assess risk and materiality
→ Develop audit strategy and plan

Performing audit procedures and gathering evidence (covered in chapter 6)
→ Gather evidence by performing audit procedures
→ Update planning and risk assessment
→ Ongoing documentation, communication and quality control

Evaluating evidence and forming conclusion (covered in chapter 6)
→ Evaluate whether sufficient appropriate evidence obtained
→ Consider materiality for reporting purpose
→ Form conclusions
→ Address subsequent events as necessary

Reporting and follow-up (covered in chapter 7)
→ Prepare reports
→ Include recommendations and responses from entity as appropriate
→ Follow up previous reports as necessary

Audit documentation (covered in chapter 8)

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[39] ISSAI 4000.15

[40] ISSAI 4000.27

[41] ISSAI 4000.28

[42] ISSAI 400.25

SAI's annual work plan for compliance audit

At this stage, the SAI selects the topics and subject matters and prepares annual or multi-annual plans for a compliance audit. The SAI decides if the engagement will be an attestation or a direct report, and whether to provide reasonable or limited assurance in the report. The SAI considers the principles of ethical significance (independence and objectivity of the auditor) and team competency, and ensures that quality control procedures are in place. The SAI also ensures the team can conduct the audit with the required documentation and communication throughout the process.

Planning individual audit

In the planning phase, the auditor examines the relationship among the subject matter, criteria, and scope of the compliance audit. In planning the audit, auditors should exercise professional judgment and consider the needs of the intended users of the audit report. Once the auditors decide on the subject matter, criteria and scope of the individual compliance audit engagement, they set the audit strategy and audit plan. The auditors should understand the entity and its internal controls, establish materiality, assess risks to the entity and plan audit procedures as part of the audit design.

Gathering audit evidence

In this phase, auditors primarily gather and document evidence to form a conclusion or opinion as to whether the subject matter, in all material respects, complies with established criteria. In some cases, auditors may need to change the scope of a compliance audit if they uncover audit evidence suggesting a need for that change. For instance, while gathering evidence, if auditors find cases indicative of fraud, they may need to modify their procedures.

Evaluating evidence and forming conclusions

At the end of the execution phase, auditors examine the evidence for sufficiency and appropriateness to form a conclusion or opinion as to whether the subject matter complies with the established criteria. At this stage, auditors consider materiality for reporting purposes.

Reporting and follow-up

The conclusion or opinion is presented in the form of a report to the intended user. Here, the auditor includes the recommendations and the entity's responses to them, as appropriate.

Illustration 2.2 on page 23 shows the possible combinations of assurance levels and types of engagements in conducting a compliance audit. The SAIs may not necessarily perform all these combinations in practice. The most common audit process is the direct reporting and reasonable assurance engagement, which is explained in this Handbook. While explaining this process, where relevant, the Handbook also includes the process for a reasonable assurance – attestation engagement.

MANAGING COMPLIANCE AUDIT AT THE SAI LEVEL
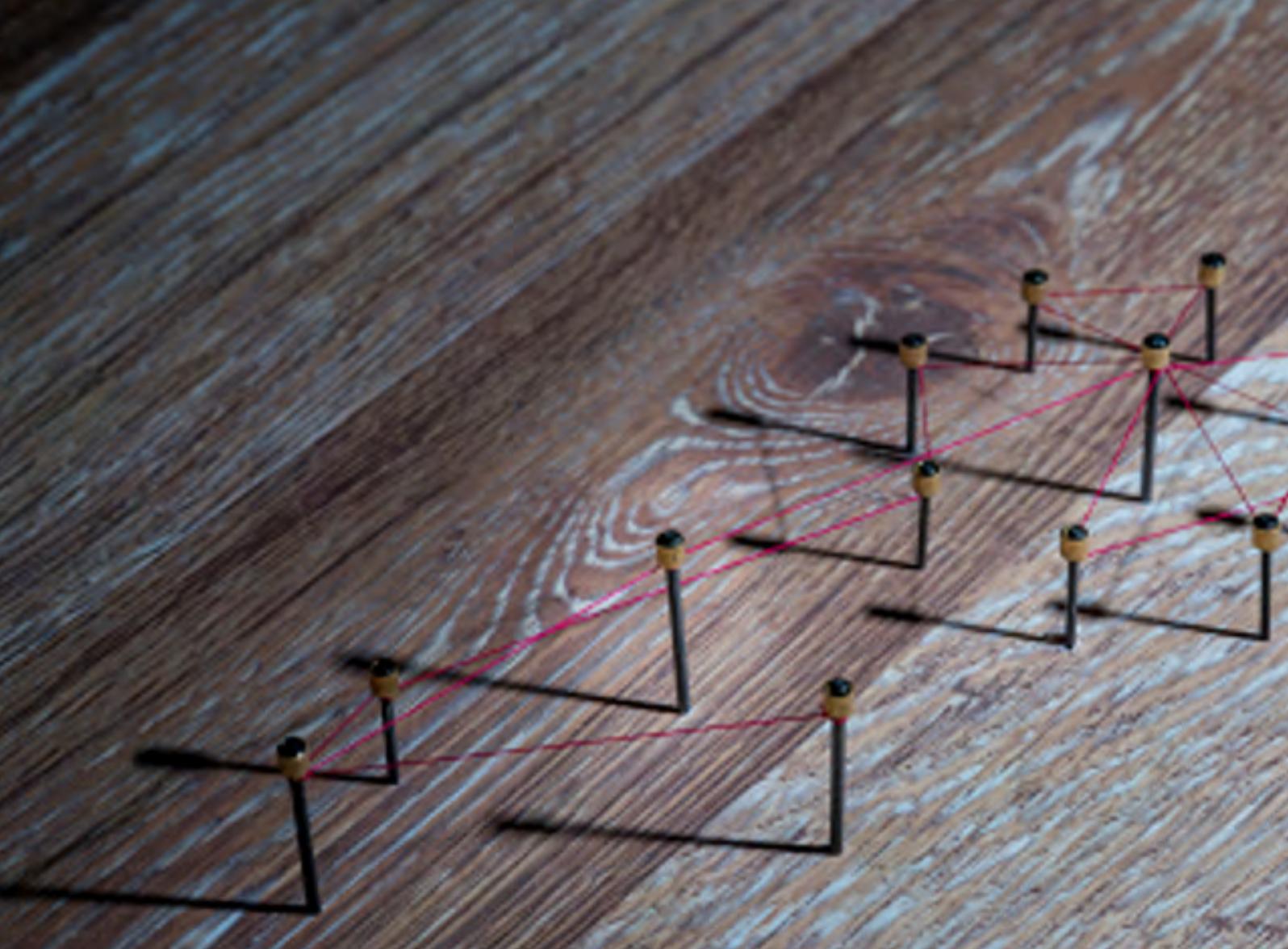
THE SAI'S ORGANISATIONAL REQUIREMENTS FOR CONDUCTING A COMPLIANCE AUDIT

3.1 Objectivity and ethics of the auditor

3.2 Audit team skills

3.3 Audit risk and materiality

3.4 Professional judgment and scepticism of the auditor

3.5 Documentation of audit work

3.6 Communication

3.7 Ensuring Audit Quality

This chapter describes the principles which are fundamental to the conduct of an audit. As the nature of the audit is iterative and cumulative, the fundamental principles are related to the SAI's organisational requirements. The SAI and the auditor should consider these principles before starting and at more than one point during the audit.[43] The SAI needs to make sure that it has established the required systems and mechanisms and has competent staff to conduct the audit, considering these elements.

ISSAI 100 - Fundamental principles of public-sector auditing and ISSAI 400 - Compliance audit **principles** highlight eight principles of the compliance audit, as shown in Figure 3.1. ISSAI 4000 includes these principles as 'the general requirements for compliance auditing.'

Implementing these general principles of compliance audit will facilitate the SAI auditors to comply with the ISSAI requirements related to an individual compliance audit engagement. This chapter explains how the SAI and its auditors could consider these principles from an organisational perspective. The relevant chapters of this Handbook will further elaborate on these, at the different application points of the audit process.

FIGURE 3.1:
Fundamental principles of compliance audit

- Protessional judgment and scepticism
- Objectivity and ethics
- Audit team management and skills
- Audit risk
- Materiality
- Documentation, communication and quality control

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[43] ISSAI 100.34

3.1 OBJECTIVITY AND ETHICS OF THE AUDITOR

ISSAI 4000.45 states, '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.' ISSAI 4000.48 states, '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.'[44]

The auditor is to demonstrate professional behaviour and integrity, be objective, possess the required professional competence and exercise due care. The auditor is also to maintain independence in fact and appearance and confidentiality regarding all audit matters.

The auditors should demonstrate objectivity in selecting their audit objectives and identifying the criteria. The auditors need to ensure that communication with stakeholders does not compromise the SAI's objectivity. The auditors also need to avoid undue influence from any stakeholders in formulating a balanced report and maintaining objectivity so that their work and report will be seen as impartial by third parties.

The SAI should establish appropriate measures to ensure that its staff follow and comply with the ethical requirements. The SAI **code of ethics** can assist the auditor in this. The SAI can refer to INTOSAI-P 10 - Mexico Declaration on SAI Independence, INTOSAI GUID 9030 - Good Practices Related to SAI Independence, and ISSAI 130 - Code of Ethics. To ensure the objectivity of the audit team members, SAIs can use predesigned templates for the declaration of no conflict/conflict of interest and conformance to the code of ethics. Based on the SAI's requirement, the SAI auditors can sign these declarations once (or, if necessary, for individual audits on a case-by-case basis) before the start of an audit cycle.

3.2 AUDIT TEAM SKILLS

ISSAI 4000.85 states that the SAI shall ensure that the audit team collectively has the necessary professional competence to perform the audit. The SAI constitutes the audit team as to collectively possess the required ability, knowledge, skills and expertise to perform the audit following professional standards. Also, ISSAI 4000.87 states that, depending on the subject matter, this may include:

- Auditing skills and abilities regarding data collection and analysis
- Legal competence
- An understanding and practical experience of the type of audit undertaken
- Knowledge of applicable standards and the authorities
- An understanding and experience of various types of entities and their operations
- The ability and experience to exercise professional judgment
- The preparation of an auditor's report that is appropriate in the circumstances

The SAI needs to assign adequately skilled resources that are available when required for the different phases of the audit process. The SAI needs 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 and appropriate audit resources. The SAI should also arrange for the auditors to maintain their professional competence through ongoing professional development.[45]

Where specialised knowledge, techniques or skills required for the audit are not available within the team, the SAI may engage external experts in different ways, such as, to provide knowledge or conduct specific work. When external expertise is required, the SAI evaluates whether the experts possess the necessary independence, competence, capabilities and objectivity. The SAI also determines whether the experts' work is adequate for the audit. The SAI is responsible for the conclusions made by the external experts as they perform audit work on behalf of the SAI.

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[44] ISSAI 4000.48

[45] ISSAI 400.45

3.3 AUDIT RISK AND MATERIALITY

ISSAI 4000.52 states, 'The auditor shall perform procedures to reduce the risk of producing incorrect conclusions to an acceptable low level.' Also, ISSAI 4000.58 states, 'The auditor shall consider the risk of fraud throughout the audit process, and document the result of the assessment.'

Audit risk is the risk that the auditor's report, conclusion or opinion may be inappropriate. A compliance audit should be performed to reduce the audit risk to an acceptable low level in the circumstances of the audit.

Decreasing audit risk includes anticipating the possible or known risks of the work envisaged and their consequences, developing procedures to address those risks during the audit and documenting which risks will be addressed and how. The auditors need to evaluate whether the scope of the work performed is sufficient. Also, when concluding, the auditors need to assess whether they have sufficient and appropriate audit evidence to support the conclusion(s) formed, based on the level of risk involved.

In an attestation engagement, the three components – the inherent risks, control risks and detection risks – are considered altogether during the evaluation of the audit risk. In a direct reporting engagement, the auditor is involved in producing the subject matter information. The auditor may apply the audit risk model in forming a conclusion on the subject matter.

ISSAI 400.47 states that auditors should consider materiality throughout the audit process. Determining materiality is a matter of professional judgment and depends on the auditor's interpretation of the users' needs. Audit risk and materiality are further explained in Part C: Chapter 5.

3.4 PROFESSIONAL JUDGMENT AND SCEPTICISM OF THE AUDITOR

ISSAI 4000.71 states, 'The auditor shall exercise professional judgment throughout the audit process.' Also, according to ISSAI 4000.77, 'The auditor shall exercise professional scepticism, and maintain an open and objective mind.'

During the audit, the auditor's attitude should be characterised by professional scepticism and professional judgment, which are to be applied when forming decisions about the appropriate course of action. Auditors should exercise due care to ensure that their professional behaviour is appropriate.[46]

Professional scepticism and professional judgment are two separate requirements, distinct in their meaning and application. However, each complements the other in the auditor's work.

Maintaining professional judgment and scepticism in compliance auditing requires the ability to analyse the structure and content of authorities as a basis for identifying suitable criteria or gaps in legislation when laws and regulations are entirely or partially lacking. It also requires the ability to apply audit concepts to a known or unknown subject matter.

Professional judgment

The auditor uses professional judgment when deciding the level of assurance, assessing risk and materiality, and defining the subject matter, scope and corresponding audit criteria. Also, the auditor uses professional judgment to evaluate the procedures necessary to gather sufficient and appropriate audit evidence, and to evaluate the procedures themselves. The use of professional judgment is crucial when analysing audit evidence and forming conclusions.[47]

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[46] ISSAI 100.37

[47] ISSAI 4000.73

Professional judgment is a skill the auditor acquires over time by obtaining relevant training and experience. That is why the application of professional judgment also means the use of the auditor's training, skill and expertise. Moreover, only an auditor with the knowledge and expertise specific to a given circumstance is expected to exercise reasonable professional judgment in that circumstance. In short, professional judgment is circumstance-based, and not every auditor is expected to be competent for every assignment.

Knowledgeable, experienced and objective persons can reach different conclusions in applying professional standards, despite similar facts and circumstances. It does not necessarily mean that one conclusion is correct and the other is wrong. Appropriate questioning is expected to understand the procedures performed and the basis for the conclusions reached.

Documentation of decisions based on the auditor's professional judgment at different stages of the audit is essential to demonstrate that a sound process was followed and to help develop a well-reasoned conclusion. When a professional judgment is challenged, documentation shows the analysis of the facts, circumstances and alternatives considered as well as the basis for the conclusions reached.

Professional scepticism

Professional scepticism is an attitude that includes maintaining an open and objective mind by being alert to conditions, circumstances and information which may indicate possible non-compliance due to error or fraud. Professional scepticism is essential when evaluating audit evidence that contradicts other audit evidence already obtained and information that brings into question the reliability of audit evidence, such as documents and responses to inquiries.[48]

Exercising professional scepticism is necessary to ensure that the auditor avoids personal bias and does not overgeneralise when drawing conclusions from observations. Besides, the auditor will act rationally based on a critical assessment of all the evidence collected.

When exercising professional scepticism, auditors maintain an open, reasonably questioning mind without being overly suspicious. The auditors do not assume that management is dishonest, nor do they believe that it is honest. Auditors always keep in mind that fraud can occur, and should not be satisfied with less than persuasive evidence, even if they believe that management is honest.

Maintaining professional scepticism throughout the audit is necessary if the auditor is to reduce the risks of:

- Overlooking unusual circumstances
- Overgeneralising when concluding from audit observations
- Using inappropriate assumptions in determining the nature, timing and extent of the audit procedures and evaluating the results thereof

3.5 DOCUMENTATION OF AUDIT WORK

ISSAI 4000.89 states, 'The auditor shall prepare audit documentation that is sufficiently detailed to provide a clear understanding of the work performed, evidence obtained and conclusions reached.'

Sufficient audit documentation is essential at every step of the compliance audit. The purpose of documenting audit work is to enhance transparency about the work performed. Also, it enables an experienced auditor having no previous connection with the audit to understand the significant matters arising during the audit, the conclusion(s) or opinion(s) reached thereon, and professional judgments made in reaching those conclusions or opinions.

Documentation needs to be sufficient to demonstrate how the auditor has defined the audit objective, subject matter, criteria and scope, as well as the reasons behind choosing a specific method of analysis. For this purpose, the auditor organises documentation to provide a clear, direct link between the findings and the evidence that supports them. Adequate documentation is essential for supervisory reviews and other quality control and quality assurance activities. Part D: Chapter 8 provides further explanation on documentation.

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[48] ISSAI 4000.78

3.6 COMMUNICATION

ISSAI 4000.96 states, 'The auditor shall communicate in an effective manner with the audited entity and those charged with governance throughout the audit process.'

Stages of communication

Communication takes place at all stages of the audit: before the audit starts, during planning, during the audit execution 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 (i.e., the entity) of the audit criteria.

ISSAI 4000.99 states, '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.'

Excellent communication with the audited entity throughout the audit process may help make the process more effective and constructive. Effective two-way communication is vital in:

- Assisting the auditor and those charged with governance to understand the matters related to the audit, with its context, and to develop a constructive working relationship. The auditor develops this relationship while maintaining independence and objectivity.
- Enhancing the auditor's sensitivity to the legislature's needs and expectations about matters communicated to others, mainly where the issues may be of broad public interest.
- Engaging the auditor with those charged with

governance to acquire information relevant to the audit. For example, those charged with governance may assist the auditor in understanding the entity and its environment, identifying appropriate sources of audit evidence, and providing information about specific transactions or events.

The communication processes

SAIs need to have a system in place that requires the auditor to ensure adequate two-way communication between the auditor and those charged with governance. If bidirectional communication is not sufficient, the auditor should take appropriate action. These may include communicating with the legislature or the relevant regulators.

The matters communicated in writing to the audited entity may include:

- The audit subject matter
- Audit criteria
- The level of assurance
- The period for the audit
- The government undertakings, organisations and programmes to be included in the audit, i.e., confirming the terms of engagement

Communicating these matters can help in achieving a mutual understanding of the audit process and auditees' operations.

The form of communication with those charged with governance throughout the audit process needs to be adapted to the conditions. The auditor considers the timing of communications and whether they are conducted orally, in writing, or both.

3.7 ENSURING AUDIT QUALITY

To ensure high-quality compliance audits, an SAI needs a System of Audit Quality Management (SoAQM) tailored to its context. Under revised ISSAI 140 — together with ISSAI 130 and 150 — establishing such a system is required when an SAI claims ISSAI compliance.

SoAQM changes quality management by focusing on system-level, risk-based measures that influence the entire audit practice. Rather than relying only on static manuals or procedures, it sets quality objectives and allows flexibility in how those objectives are achieved. Its risk-based approach helps the SAI identify issues early and prioritise responses. Monitoring, remediation and evaluation processes enable timely correction of deficiencies and support continuous improvement.

System-level quality risk management, monitoring and evaluation drive quality at the engagement level. In addition, audit supervisors or directors may identify engagement-specific quality actions — for example, additional review steps, closer supervision, or a need for consultation — when specific risks apply only to a particular audit.

Part D: chapter 9 provides further explanation on quality management at the engagement level.

THE SAI'S ANNUAL WORK PLAN FOR COVERAGE OF COMPLIANCE AUDIT

4.1 Setting the strategic priorities of the SAI

4.2 Identification and prioritisation of potential audit tasks

4.3 The SAI's annual or multi-annual work plan

4.4 Considerations before initiating an individual compliance audit

SAIs generally plan their audit work on an annual or multi-annual basis. Based on the SAI's legal framework, the plan specifies the types of audit it can conduct: financial, compliance or performance. The SAI considers the resources available to it while it undertakes the audits for a given period. It sets aside the necessary resources first to accomplish the mandatory audit tasks. The remaining resources available determine the extent to which the SAI can include additional audit tasks in its annual or multi-annual work plan. This chapter describes the process an SAI can follow to determine the audit tasks and to prepare an annual or multi-annual plan for a compliance audit. Although the chapter focuses on the compliance audit, a similar process can be used for other types of audit as well.

ISSAI 4000.64 includes the selection of audit coverage as part of the general requirements for a compliance audit. It states, '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).'

Some SAIs perform audits on request from the legislative body, e.g., Parliament, while others have the option to select the coverage of their compliance audits or both. Where the SAI has discretion to choose coverage, it may establish a system to recognise significant audit issues and the areas with potential risk of non-compliance. The steps to identify the possible audit tasks for compliance audits (i.e., subject matters) and, accordingly, to make an annual plan may typically involve:

- Setting the SAI's strategic priorities;
- Identifying and prioritising the potential audit tasks; and
- Preparing an annual or multi-annual work plan.

4.1 SETTING THE STRATEGIC PRIORITIES OF THE SAI

The SAI generally derives the strategic priorities from the policy and risk review. The review helps ensure that the SAI selects audit tasks that best reflect the risks, public interests and potential for the SAI to add value, and that contribute to the country's accountability framework. Strategic priorities provide a high-level orientation for the annual or multi-annual work plan. SAI priorities could include, among others, policy areas requiring particular attention, such as social security and housing, as well as emerging risks arising from the evolving environment in which the SAI operates, such as big data and new technologies. Priorities could also include cross-cutting audit topics, such as gender, climate change and procurement.

The policy and risk review takes into account the country's strategic development priorities and goals, the stakeholders' interests, audits performed in the other countries that the SAI considers pertinent, as well as developments in the professional audit practices. The policy and risk review should, in particular, consider the pre-legislative process to determine the optimal delivery time of audit reports to ensure the best possible impact. In performing the policy and risk review, the auditor may consider, among others, the following:[49]

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[49] ISSAI 4000.67

ILLUSTRATION 4.1:
Policy and risk review

REVIEW OF:	IN THE AREAS OF:	OUTPUT:
Stakeholders' priorities and interests	→ Public or legislative interests or expectations → Strategic goals of the country, e.g., achievement of Sustainable Development Goals → The interest of citizens (the SAI may provide options on its website to gather citizen input) → Donors' or funding agencies' interests or expectations → Interests of beneficiaries of public funds → Media coverage on issues of public interest → Non-compliance signalled by third parties	The output is a list of the issues and risk areas, linked to the stakeholders' priorities and interests.
Changes to the legal framework and other developments in the area	→ Developments and changes in the legal framework in different areas → Significance of specific provisions of the law, and their interpretation by the entities → Principles of good governance → Other significant changes and developments in the different areas → Roles of different public sector bodies, the situation and changes to that → Rights of citizens and public sector bodies → Potential breaches of applicable laws and other regulations, as well as financing agreements with donors that govern the entity's activity, or the public debt, public deficit and external obligations → Projects with significant public funding	The output is a list of issues and risk areas linked to the recent changes and developments in the country.
Results of recent audits and developments in the audit	→ Non-compliance with internal controls or the absence of an adequate internal control system → Findings identified in the SAI's previous audits → Works of other SAIs and similar entities → Recent developments in the audit profession → Mandate and audit coverage of the SAI	The output is a list of issues and risk areas identified in recent audits.

The policy and risk review maps the main developments in the country and identifies the relevant high-level issues and risk areas. When performing the review, the auditor may analyse budget proposals, related public-sector publications, and evaluation reports. Engaging with stakeholders and participating in discussions across different forums may enrich the auditor with valuable information, to form the basis for selecting the appropriate and timely subject matters and to reduce the risk of auditing low-risk areas. The auditor may often come across examples of non-compliance in connection with other types of audit performed by the SAI. It can, therefore, be useful to include such findings in the risk assessment process for the coming year.

The accumulated outputs of the policy and risk review process are a list of the SAI's strategic priorities. The SAI could align these priorities with its strategic plan to achieve the yearly operational targets. Besides audit tasks, the SAI could consider establishing a strategic approach to other activities it would like to accomplish, as an organisation, in the medium and long term. These may include, among others, developing staff capacity, strengthening compliance audits, or ensuring that a certain percentage of SAI staff obtain a professional qualification.

4.2 IDENTIFICATION AND PRIORITISATION OF POTENTIAL AUDIT TASKS

SAIs should consider their strategic priorities while identifying possible audit tasks. The potential audit tasks include a list of proposed audit topics, an estimate of resources required for each and information on their relative significance. The audit tasks could be identified by following a bottom-up and top-down approach, and the SAI should document the process.
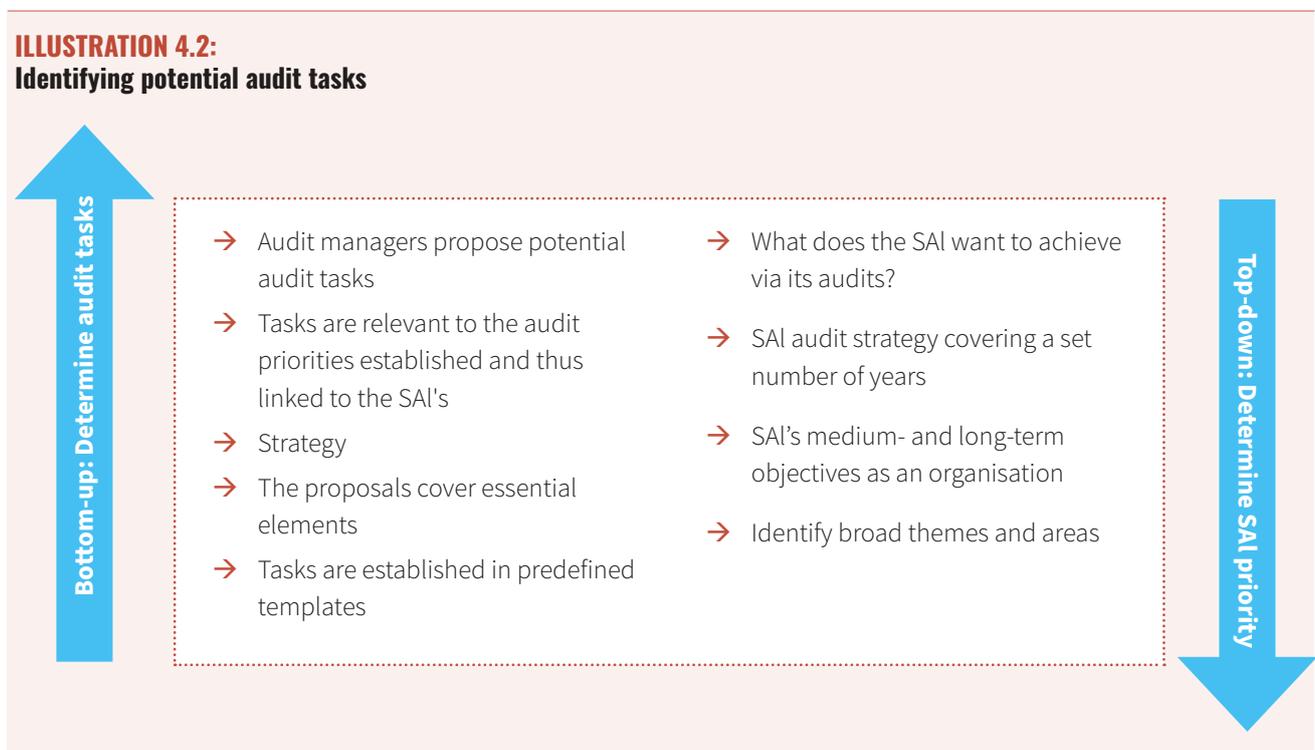
The top-down approach flows from the SAI's strategic plan, which spans a set number of years. The strategic plan is operationalised in multi-annual and annual plans and priorities. These priorities determine what the SAI wants to achieve as an organisation through its audits as short-term, medium-term and long-term objectives. In this process, the SAI identifies broad themes and areas of significance of national or international interest, e.g., information technology, the Sustainable Development Goals, and the environment.

In the bottom-up approach, the audit managers propose potential audit tasks. These are generally relevant to the audit priorities established and thus are related to the SAI strategy.

Illustration 4.2 explains the key features of the two approaches.

ILLUSTRATION 4.2:
Identifying potential audit tasks

Bottom-up: Determine audit tasks

→ Audit managers propose potential audit tasks

→ Tasks are relevant to the audit priorities established and thus linked to the SAI's

→ Strategy

→ The proposals cover essential elements

→ Tasks are established in predefined templates

Top-down: Determine SAI priority

→ What does the SAI want to achieve via its audits?

→ SAI audit strategy covering a set number of years

→ SAI's medium- and long-term objectives as an organisation

→ Identify broad themes and areas

The auditor can use the template provided in Exhibit 4.1: Documenting a potential audit task to facilitate the bottom-up approach to identifying the tasks. Also, an example of the process for categorisation of entities based on risk value is provided in Appendix 4-A. The key aspects of identifying an audit task include the following.

Assessing priority

The SAI compares all proposed tasks with the strategic priorities for the respective planning period and assesses the extent to which they cover the priorities. This analysis identifies the audit tasks best suited to address the strategic priorities and the priorities that have not been sufficiently covered by the proposed audit tasks.

Such an analysis should use a set of criteria such as the relevance to the strategic priorities, significance of the risks, political and public interest and the potential added value the audit would generate. The latter can include, among others, considerations of economic importance, past coverage and auditability. This analysis should also rank the proposed audit tasks and document the process. The relevance of an audit task to the strategic priorities could be assessed as low, medium or high.

Assessing risk

The risk associated with a proposed audit topic could be assessed as low, medium or high, depending on the likelihood of occurrence of the main factors identified and their potential impact. An auditor can document the risk assessment of a topic using Illustration 4.3.

ILLUSTRATION 4.3:
Determining the importance of risks

Audit task:		
	Likelihood of occurrence	
Potential impact	Low	High
Substantial	Medium risk	High risk
Minimum	Low risk	Medium risk

Assessing political and public interest

The tasks considered for audit should be of interest to the SAI's primary stakeholders, such as Parliament. The auditor deliberates on the decisions made by Parliament, the reports and the policy documents it has produced as the possible sources of information. At the same time, the auditor bears in mind the interests of the executive and the media, as well as the impact on the lives of citizens. For each proposed audit task, the auditor should determine the level of public interest (low, medium or high).

Assessing potential added value

- SAIs can consider the topic's potential added value in terms of its economic importance. Also, SAIs need to assess whether the audit report would provide new and useful information to the users. For this, SAIs can take into account audits, control reviews, and evaluations that have recently been carried out or are planned by SAIs and other agencies. The SAI may prioritise areas and topics that have never been audited, were partially audited, or were audited many years previously.

- Consider the potential impact in terms of identifying weaknesses and making recommendations.
- Timeliness is a crucial element. The selection of topics should align with the timing to contribute to changes, such as significant reforms or the introduction of new initiatives. A delayed report will not influence events, and therefore, it loses its relevance.
- Auditability or feasibility should also be considered and assessed; that is, whether it is technically or practically possible to carry out the audit and whether the SAI has the capacity and skills needed. External expertise, might be needed, for example.

For each task, the SAI should translate the result of the assessment of these four pre-established criteria into a priority ranking. The SAI could allocate the degree of priority to audit tasks based on the total score achieved. The topics are then ranked based on their level of significance based on the overall score. Illustration 4.4 proposes how the auditor can allocate the degree of priority to a particular audit task using the total score.

ILLUSTRATION 4.4:
Priority ranking of a task

Audit task:							
Priority		**Risk**		**Public interest**		**Added value**	
	Score		**Score**		**Score**		**Score**
Low	1	Low	1	Low	1	Low	1
Medium	2	Medium	2	Medium	2	Medium	2
High	3	High	3	High	3	High	3
Total score:							

4.3 THE SAI'S ANNUAL OR MULTI-ANNUAL WORK PLAN

The yearly or multi-annual work plan includes information on the audit tasks to be carried out, a brief description of each job, the human resources and other resources (e.g., travel costs, expertise needed) to be allocated to each task, and the intended implementation and reporting calendar.

Establishing an annual or multi-annual work plan is based on each SAI's internal process. SAIs may consider doing the following:

- Determine the total staff resources available and establish the standard number of days (excluding the yearly non-workdays as regulated by the SAI) for full-time staff.
- From the total staff resources available, deduct the necessary resources for mandatory and other recurrent tasks, including non-audit work. Allocate other resources for these tasks.

- After determining the remaining staff and other resources, identify the number of potential audit tasks, ranked with the highest priority, that the SAI could carry out in the given planning period.

The SAI may apply these considerations and document the process using Exhibit 4.2: Establishing the annual or multi-annual work plan.

The SAI might consider setting realistic timelines and spreading the workload over the planning period. To this end, SAIs should ensure that the resources allocated to each task are sufficient in both quantity and quality. The SAIs can take into consideration a margin for contingencies and unforeseen events that could affect the plan during the implementation of the tasks.

The SAI should regularly monitor the implementation of the annual or multi-annual work plan to inform management on progress made, resource utilisation, milestones attained, objectives achieved, and work still pending. The SAI could establish a half-yearly reporting system for the implementation of the annual work plan. Based on the monitoring results, the plan can be revised if the underlying assumptions change, the priority ranking is no longer valid or other reasons for needed change become apparent.

4.4 CONSIDERATIONS BEFORE INITIATING AN INDIVIDUAL COMPLIANCE AUDIT

After the SAI has established the organisational requirements for conducting compliance audits (explained in Chapter 3), prepared its annual work plan and allocated the required resources, it will start performing the audits. At this point, the SAI has also identified the prioritised subject matters and topics for compliance audits. Before the SAI's compliance audit teams begin planning and performing the audits according to the SAI's annual work plan, the SAI management may like to ensure that the teams apply the audit methodology consistently in all compliance audits. For this, the SAI management needs to make informed choices on when to conduct a direct reporting engagement or an attestation engagement, and when to provide reasonable or limited assurance in its audit reports. Accordingly, the management could communicate these options to the auditors and the respective functional heads of compliance audit (or, as appropriate, in the respective SAIs).

Direct reporting engagement or attestation engagement

The availability or unavailability of the subject matter information leads the auditor to decide whether to carry out an attestation engagement or a direct reporting engagement. The SAI would choose to conduct attestation engagements for subject matters and prioritised topics where the responsible party or entity prepares the information, and the auditor would attest to that. In the absence of such information, SAIs would conduct direct reporting engagements. As per ISSAI 4000, these two approaches may

differ in their audit sampling and the risk assessment processes.

Generally, the availability of the subject matter information (prepared by the entity) is limited for a compliance audit. In most cases, the auditor will determine the subject matter and provide a conclusion on that. With this in mind, the SAI may choose to conduct its planned compliance audits as direct reporting engagements except where the information to attest is available.

Reasonable assurance or limited assurance

ISSAI 4000.121 states, '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.'

While determining the scope and subject matter of an audit, the auditor considers the level of assurance provided. The SAI decides on whether to conduct a limited or a reasonable assurance audit by considering the following:

- Needs of the intended user
- Availability of and access to information
- Extent of audit procedures
- Competency of the auditors

Needs of the intended user

The SAI has to assess the needs of the intended users of the audit report to determine which type of assurance is most appropriate. The assessment process requires an understanding of the decisions made by the users and the kind of information they use for decision-making. Some SAIs have mandated requirements which already define the level of assurance they should provide in their reports.

Availability of and access to information

Providing reasonable assurance requires more extensive audit work.[50] A reasonable assurance engagement requires the auditor to have access to the systems and processes used in the subject matter (e.g., internal controls of an entity), and therefore,

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[50] ISSAI 4000.34

demands more information than a limited assurance audit, which focuses on a narrower area. Thus, limitations on accessing the data would likely lead to a limited assurance audit.

The extent of audit procedures

In a reasonable assurance engagement, the auditor is likely to perform tests of controls and detailed substantive testing to reach an overall conclusion about the subject matter. The auditor can identify a sample of transactions that is representative of the total population and extrapolate the results of sampling to the whole. The auditor is likely to evaluate the systems and processes of the subject matter to reach an overall conclusion in a reasonable assurance engagement.

In a limited assurance engagement, the aim is to obtain a level of assurance meaningful to the intended users. The auditor gathers sufficient and appropriate evidence to address the engagement objective; however, the procedures are limited compared with what is necessary for a reasonable assurance engagement.[51]

Competency of the auditors

Reasonable assurance and limited assurance engagements both would require competent staff. ISSAI 4000.85 states, 'The SAI shall ensure that the audit team collectively has the necessary professional competence to perform the audit.'

SAIs can use an audit team competency matrix to map their auditor competency. Based on professional judgment, the matrix could include assessing whether the members demonstrate the required cross-cutting and functional competencies and have experience in conducting compliance audits, including the sector or area under audit. Some SAIs may have fixed audit teams with designated supervisors for one audit cycle year. In that case, instead of selecting audit teams for each engagement, it is sufficient (and manageable) to make the selection of teams based on the competency matrix once a year. If there is a change in the team composition, it can be updated periodically as necessary.

Appendix 4-B explains the four stages of a compliance audit and how the auditor's tasks differ at each of the steps in different types of compliance audits.

Considering these issues and the SAI's context, the SAI management may decide that, in general, the SAI's compliance audit engagements will be direct reporting - reasonable assurance engagements. And based on this decision, SAI teams will initiate the individual audits as direct reporting engagements. Part C of this Handbook explains the methodology for conducting such engagements.

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[51] ISSAI 4000.201

CONDUCTING COMPLIANCE AUDIT

PLANNING A COMPLIANCE AUDIT

5.1 Developing the audit strategy

5.2 Developing the audit plan

5.3 Documenting and ensuring the quality of the audit strategy and audit plan

This chapter explains the planning of an individual compliance audit engagement. There are two steps in planning a compliance audit. In the first step, the auditors develop the overall **audit strategy** for the audit's scope, emphasis, timing and conduct. In the second step, based on the strategy, auditors prepare an **audit plan** that outlines a detailed approach and specific steps for the nature, timing, and extent of procedures to be performed, and the reasons for selecting them. The chapter includes

suggested working paper templates for the auditors to document the development process of the audit strategy and the plan.

The planning activities will vary, among others, with the circumstances of the audit, the complexity of the underlying subject matter and the criteria.

In planning a compliance audit, the SAI auditors generally consider the following elements:

Characteristics of the audit	**Scope, subject matter and criteria**	**Intended users**	**Understanding of the entity**
Entity's control environment and internal control	**Components of audit risk**	**Materiality**	**Relevance of fraud risk**
Internal audit function and coverage	**Resources necessary for the audit**	**Nature and extent of experts required**	**Timing and nature of communication**

These elements are illustrated in Figure 5.1 as the generic steps of a compliance audit planning process.

ISSAI 4000.137 states, '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 schedule for the audit work.' The process for developing the audit strategy and audit plan is explained in the following sections.

FIGURE 5.1:
Audit planning process

AUDIT STRATEGY	STEPS TO DEVELOP THE AUDIT PLAN				AUDIT PLAN
Audit objective	Understand the entity	Understand the internal control	Identifying and assessing the risks	Determine materiality	Design audit procedures for risks
Subject matter, scope, criteria	Identify the entity or activities	Control activities	Inherent risks	Qualitative materiality	Nature, extent and timing of procedures
Type of engagement	Laws, regulations governing the entity	Entity's assessment of risks	Control risks	Quantitative materiality	
Level of assurance	Policies, plans, strategic plans	Control environment	Fraud risks	Set materiality threshold	Determine required resources
Audit team composition	Media reports, internal audit	Information and communication	Determine the combined risks		Finalise audit schedule
Quality control		Monitoring	Impact, likelihood of the risks		
Communication			Risk register		Audit strategy and audit plan memo

5.1 DEVELOPING THE AUDIT STRATEGY

The audit strategy serves as the basis for deciding whether it is possible to execute the audit. The audit strategy describes what to do, and the audit plan describes how to do it. The purpose of the audit strategy is to design and document the overall decisions made by the auditors. It may contain the following[52]:

ELEMENTS OF AN AUDIT STRATEGY

1. Characteristics of the compliance audit

2. The audit objective

3. Subject matter, scope, criteria

4. The entities covered by the audit

5. The type of engagement

6. The level of assurance to be provided

7. Composition of the audit team

8. Quality control mechanisms

9. Communication

10. Reporting responsibilities
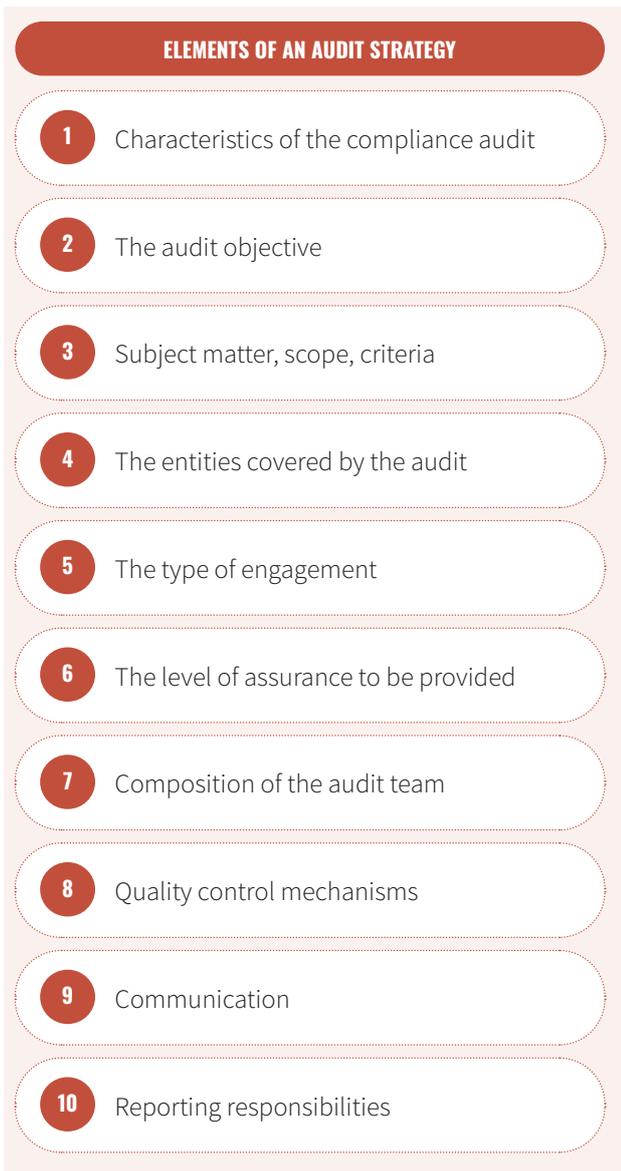
An audit strategy facilitates the coordination between the audit team members and the SAI on the audit approach. The audit team develops the audit strategy based on the SAI's organisational requirements for conducting an audit.

Characteristics of the compliance audit

The audit team takes into account the SAI's mandate and strategic plan when determining the characteristics of an audit. The team includes an introductory description of the audit and a background.

The audit objective

The audit objective determines what the auditor aims to answer in the audit. The auditors ensure objectivity in formulating the audit objectives, including identifying the criteria. Audit findings depend entirely on the purposes of the audit, and findings are complete to the extent that the audit's goals are satisfied. The audit objective should be answerable and should identify the audit subject matter, the entity or activities under the audit.

The subject matter, scope and criteria

The subject matter, scope and criteria are interrelated. The auditor scopes the subject matter in such a manner that it is sufficiently covered to conduct a meaningful audit and to add value for the intended users.

Subject matter

Section 2.2 (Chapter 2) introduced the concept of the subject matter. The SAI's annual compliance audit plan may identify and include audit subject matter. The subject matter should be identifiable and assessable against suitable audit criteria. It should be of a nature that enables the auditor to conclude with the required level of assurance.

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[52] ISSAI 4000.139

Scope

Audit scope refers to the area, extent and period covered in the audit of a given subject matter. Scoping involves narrowing the audit subject matter to relatively fewer issues of significance that pertain to the audit objective, and that can be audited with the resources available to the audit team. In a multi-entity or thematic compliance audit, the scope includes identifying the entities that will be included in the audit. Clearly defining the audit scope is important for determining the budget, human resources and time required for the audit, and in deciding what the auditor will include in the report.

The statement of scope should be clear about any areas that are related to but not included in the audit. The scope of a compliance audit may change while conducting the audit if the auditors identify material information that makes it necessary to reconsider the scope. Section 2.2 of Chapter 2 explains scoping of a subject matter with an illustration.

Criteria

Section 2.3 (Chapter 2) explains authorities and criteria. For a direct reporting engagement, the auditor must ensure that there are corresponding audit criteria. The subject matter and relevant audit criteria might already be defined by the SAI's mandate or national legislation. In an attestation engagement, the audit criteria are implicitly given by the presentation of the subject matter information, based on which the information has been prepared. In such a case, the auditor needs to conclude on the correctness of the criteria implicit in the subject matter information.

The case scenario in Illustration 5.1 below demonstrates the relationship between the subject matter, scope and criteria.

ILLUSTRATION 5.1:
Relationship between subject matter, scope and criteria

Example: Identifying the subject matter, scope and criteria	
Case	
The audit aims to review the National Health Service's (NHS) procurement policy against the national procurement requirements, and the extent to which the procurement practices followed by the NHS comply with the guidelines for government procurement. In this respect, the audit will cover the procurement policy as well as the planning and sourcing stages of the procurement life cycle. It will encompass an assessment of all procurement activities for the 18 months from 1 July 20XX to 31 December 20XX. The subject matter, the scope and the audit criteria are:	
Subject matter	The activity, project, process or programme the auditor decides to examine. In this case, the subject matter is the procurement practices of the National Health Service.
Audit scope	Audit scope explains the coverage and extent of the audit examinations. In this case, the audit scope is the planning and sourcing stages of the procurement life cycle, covering all procurement activities for the 18 months from 1 July 20XX to 31 December 20XX.
Criteria	Audit criteria are the benchmarks used to measure the subject matter. Criteria are derived from authorities (e.g., laws, regulations, policies, and guidelines). In this case, the criteria will derive from the: → Section xx of the guidelines for government procurement → Section xx of the national procurement policies

The entities covered by the audit

The subject matter relates to a theme or an entity. Thematic subject matter may include multiple entities across the government; for example, the environment and procurement. They require careful planning and execution of the audit to ensure that all entities related to the subject matter are adequately covered and that an audit conclusion can be reached.

The type of engagement

The team decides whether the audit is an attestation engagement or a direct reporting engagement, considering the subject matter. The team follows the decisions made by the SAI management, as explained in section 4.4 (chapter 4).

The level of assurance to be provided

In most cases, the audit team decides on a reasonable assurance compliance audit engagement. The team considers the subject matter and the SAI management decisions, as explained in section 4.4 (chapter 4).

Composition of the audit team

The team should be composed of adequately skilled resources to conduct the audit. The audit team determines if there is a need for external experts for skills not available within the team. The team considers how the SAI manages the audit team's skills, as discussed in section 3.2 (chapter 3).

Quality control mechanisms

The team takes into account the quality control mechanism for the audit, as discussed in section 3.7, to ensure a high-quality audit is undertaken.

Communication

The team determines how it will communicate with the auditee and those charged with governance throughout the audit process.

Reporting responsibilities

The team determines to whom and when the reporting will take place, and in what form the team will prepare the report.

As required by ISSAI 4000.137, the audit team can document the audit strategy covering all elements with the working paper template provided in **Exhibit 5.1.**

Note: In a simpler audit, a small team may conduct it. With a smaller team, coordination and communication between team members and the SAI management are easier. Establishing the overall audit strategy in such cases need not be a complicated or time-consuming exercise. When documenting the audit strategy, the team can modify Exhibit 5.1 to reflect the specific context of the audit, subject matter, complexity, and criteria.

5.2 DEVELOPING THE AUDIT PLAN

This section describes the process of developing an audit plan, including the required documentation of the process with working paper templates. The output of the planning phase is a written plan for carrying out the audit fieldwork. The plan describes the potential risks of non-compliance to the entity and the required audit procedures for the identified risks.

The audit strategy provides essential input to the audit plan by defining the audit objectives, scope, subject matter and criteria. Planning is an iterative process throughout the audit. The auditors may need to modify the objectives, scope, methodology, and timing as the audit progresses. The audit plan includes the following elements (ISSAI 4000.140):

THE ELEMENTS OF AN AUDIT PLAN

1. An assessment of risk

2. An assessment of internal controls relevant to the audit

3. The audit procedures designed as a response to the risks identified

4. Nature, timing and extent of planned audit procedures

5. When the audit procedures will be performed

6. The potential audit evidence to be collected during the audit

The assessment of the risks and internal control requires having an understanding of the entity or the subject matter and its internal control systems, and identifying the inherent risks, control risks and risks due to fraud. The auditor then applies the set materiality level to the risks identified and designs the audit procedures for the identified risks. While conducting the audit, the auditor performs the audit procedures according to the audit plan and gathers sufficient and appropriate audit evidence to fulfil the audit objectives and to make a conclusion on the subject matter.

Understanding the entity or the subject matter

ISSAI 4000.131 states, '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 the audit.'

The objective of understanding the audited entity and subject matter is to identify the risks of non-compliance within the entity, which will determine the audit approach.

If it is a thematic compliance audit (e.g., procurement, gender), that covers more than one entity, the auditors obtain an understanding of all entities whose activities fall within the audit scope. Some SAIs conduct a compliance audit of the utilisation of a fund that is used by more than one entity. In such audits, the auditor may need to consider the

strategies, operations and governance of all relevant entities utilising the fund.

The auditor should understand and evaluate the activities and operations directed towards the attainment of the audited entity's goals and objectives, which, in turn, should address all of the entity's compliance requirements. Also, the auditor evaluates that the legal acts applied to the entity's operations and other authorities, such as administrative policies, internal procedures, instructions and orders, do not contradict the normative legal acts.

Understanding the entity or the subject matter

→ Relevant business

→ Laws and regulations

→ Nature of entity operations

→ Governance arrangements

→ Objectives and strategies

→ Performance measures

To obtain an understanding of the entity and its environment, the auditor may consider the relevant business, laws and regulations, other external factors, the nature of the entity's operations, governance arrangements, objectives, strategies, and performance measures.[53] The auditor may acquire an understanding of the following:

LEGAL FRAMEWORK	Legal basis for the activity, and relevant parts of the financial regulation, implementing rules and regulations.
ORGANISATION AND GOVERNANCE	Of the subject matter, activity and audited entity, including operational structure, resources, organisation chart and management arrangements.
BUSINESS PROCESSES AND OPERATIONS	The key policies, objectives and strategies, locations, and types, volume and values of the programmes, functions and projects.
BUSINESS PROCESS ANALYSIS	Key businesss process maps, flowcharts, risk and control matrices, process narratives for an overview of functions and operations of the entity or the subject matter.
BUSINESS AND OPERATIONAL RISKS	Related to the entity's objectives and strategies that may result in material non-compliance.
PERFORMANCE MEASURES	Performance indicators, variance analysis to consider whether pressures to achieve performance targets may result in management actions that increase the risk of non-compliance.

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53 ISSAI 4000.133

A thorough understanding of the audited entity, as outlined in laws, policies, or standards, helps auditors to recognise when non-compliance has occurred and to obtain evidence through performing the audit procedures. The audit team can document the process of understanding the entity and its environment with the suggested working paper template provided in Exhibit 5.2.

Understanding the internal control system

ISSAI 4000.134 states, 'The auditor needs to obtain an understanding of the entity's internal control relevant to the audit.' The auditor identifies the internal controls in place to reduce the risk of non-compliance with the criteria in the subject matter. By using professional judgment, the auditor decides whether the control is relevant to the audit or not.

Internal control is a necessary process – a series of actions that permeate an entity's activities – and is affected by entity management and personnel. It is composed of policies, structures, procedures, processes and tasks that help ensure that management directives are carried out and enable the audited entity to respond appropriately to any risks of non-compliance. Internal control is designed to address the risks and to provide reasonable assurance that, in pursuit of the entity's mission, it:

- Fulfils the accountability obligations;
- Complies with the applicable laws and regulations;
- Safeguards resources against loss, misuse and damage; and
- Executes orderly, ethical, economic, efficient and effective operations.

The auditor makes a preliminary evaluation of the internal control system to:

- Gain an understanding of the extent to which improvements in internal control systems are being made year-on-year;
- Conclude on the effectiveness of the internal control system and identify the control risks; and
- Design the nature, timing and extent of audit procedures.

The auditor may obtain an understanding of the following five interconnected components of the internal control system relevant to the audit[54]:

1. The control environment
2. The entity's risk assessment process
3. Information and communication systems
4. The control activities
5. The monitoring of the controls

FIGURE 5.2:
Internal control framework

Monitoring

Information and communication

Control activities

Risk assessment

Control environment

Generally, the controls are established within the entity to reduce the risks. In other words, the entity's 'assessment of risk' in the organisations and its operations creates the need for controls. After the entity identifies the risks it faces, it needs to design controls (e.g., approval, authorisations, verifications, reviews, segregation of duties) to mitigate those risks, and these controls need to be shared among the staff throughout the organisation (information and communication systems). Those responsible for managing the entity should respect the rules and not override controls to ensure the entity's 'control environment' is efficient and effective. The entity management needs to set up a process for 'monitoring' of controls to ensure that the controls are working as planned.

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[54] ISSAI 4000.135

The audit team can document the understanding of the entity's internal control system with the suggested working paper template provided in **Exhibit 5.3**.

(Note: For a small entity, and if, in the auditor's professional judgment, the entity does not have a matured internal control system covering the five elements, applying Exhibit 5.3 to document the internal control system might not be appropriate. In such cases, the auditor can document the understanding of the internal control system following a different approach as explained below.)

Internal control for a small entity or subject matter

Small entities may not be able to apply all five elements of the framework for the internal control system. They neither have a monitoring system in place nor a formal risk assessment system. Some entities are so small (or their control systems are so weak) that they often do not have any formal controls in place at all. A large and well-organised government entity can manage the whole spectrum of the internal control framework because they have the required financial and human resources, leadership and a highly motivating fear of the authorities constantly checking its compliance. These factors allow them to establish the control framework in full. In smaller entities or entities with weaker control systems, rather than covering the full details of the five elements, the auditors may ask the questions in Illustration 5.2 to understand their internal control system.

The auditor can document the internal control system using this questionnaire instead of Exhibit 5.3, for the entities or subject matters that do not have an established system of internal control.

ILLUSTRATION 5.2:
Internal control questionnaire for a small entity or subject matter

Components of internal control	Questions to ask
Control activities	→ How does the entity ensure that it complies with the relevant rules and regulations for its functions? What mechanisms does it have for that? → How does the entity ensure that its existing control mechanisms for complying with the rules and regulations are operating effectively and efficiently?
Risk assessment	→ How does the entity determine that specific control activity(ies) is/are essential to ensure compliance?
Information and communication	→ How does the entity notify its staff responsible for operations that a certain control activity or mechanism is required for compliance?
Monitoring	→ What is/are the process(es) used by the entity to ensure that the control activity(ies) is/are performed correctly and consistently to ensure compliance?
Control environment	→ What is the attitude of entity management about the control mechanisms? *(The control environment is a summary of the other four components.)*

Identification and assessment of risks

Risk assessment guides the auditor to focus on the critical issues of the subject matter or entity under audit, while considering resource and time constraints. The outcomes of the risk identification activities are documented using the 'understanding of the entity' and 'understanding the entity's internal control system' templates. It includes identifying the inherent risks, control risks, and determining the detection risks. The audit risk model helps the auditors to determine how comprehensive the audit work should be to attain the desired level of assurance for their conclusions on the subject matter.

In an attestation engagement, the audit risk has three components[55]:

1. The subject matter's inherent risk (IR); the risk of material non-compliance occurring regardless of existing internal controls

2. The control risk (CR): the risk that the relevant internal controls associated with the entity are inappropriate or do not work properly to prevent material non-compliance

3. The detection risk (DR): the risk that material non-compliance will not be detected by the auditor, which will lead to an incorrect conclusion or opinion.

Risk assessment activities include, among others, inquiry (with management, key officials, internal audit), inspection (of entity premises, internal documents and records, website and media, previous audits), observation (of the entity's operations being carried out) and analysis (of financial and non-financial information with analytical procedures).

Identifying subject matter's inherent risk (IR)

Auditors estimate the inherent risk based on their understanding of the entity's activities and operations. Inherent risk is described as the 'risk in the absence of controls.' In audit terms, inherent risk is the risk related to the nature of the activities, operations and management structures where non-compliance will occur if not prevented, detected and corrected by the internal control. The auditor can determine the inherent risks by considering the following:

- Generic risks of the entity or subject matter
- The 'reverse of criteria' risks
- Predicting 'what could go wrong'
- Previous audit results
- Entity's risk assessment process

To identify the inherent risks, the audit team may hold a brainstorming session and consider all the conditions and events at the entity that may indicate the risks of non-compliance.

Generic risks of the entity or subject matter: It is the risks that arise every time the entity takes action. During the risk identification and assessment process, the auditor considers the risks embedded within the function of the entity or subject matter as generic risks.

Reverse of criteria risk: This is a risk arising from the premise that the entity might not comply with the authorities, i.e., the audit criteria. When the auditor analyses criteria applicable for a subject matter or entity, the reverse of that criterion might lead the auditor to envision the potential risks of non-compliance.

Example: The reverse of the criteria risk

An auditor is evaluating whether the entity meets a regulation (audit criteria) that requires all beneficiaries of a government support programme, operated by the entity, to have an annual income below the poverty level. The criterion here is the poverty level set by the regulation. The reverse of this criterion (i.e., the inherent risk) is that there are beneficiaries in the programme who are above the set poverty level and therefore are not eligible for the programme support. The inherent risk is that those who should benefit from the programme are not benefiting, and that people above the set poverty level could be receiving resources intended to help the poor.

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[55] ISSAI 4000.54

Predicting what could go wrong: The auditor exercises professional scepticism in anticipating the risks of non-compliance in the subject matter under audit. Assessing the inherent risks requires the auditor to analyse the entity or the subject matter and forecast what could go wrong within it. The auditors consider the criteria against which they are evaluating the subject matter and seek to determine the purpose of the criteria. What did the lawmakers or authorities intend to achieve with that law or regulation? The auditor can then envision whether the event that the regulators were trying to prevent might have occurred.

Previous audit results: The previous audit reports can also be a good measure of risk assessment in the area at the time of audit planning. The auditor should follow up with the recommendations to confirm if the previous incidents of non-compliance were corrected or addressed by the entity. The auditor can review the prior working papers to set linkages with the current risk assessment process.

Entity's risk assessment process: The entity's risk-assessment process, if it exists, can also serve as a source of information on the risks of non-compliance. The entity's annual plan may identify the critical risks specific to particular areas, and its yearly activity report provides an overview of the critical risks encountered and their impact on achieving the entity's objectives. However, the auditor should exercise professional scepticism, as risks identified by the audited entity may not address those that are important for audit purposes, and such information may be biased. The auditor can also consider the entity's internal audit report, if it exists, to identify potential areas of concern.

By noting down all the potential areas identified, the auditor will have a list of inherent risks of non-compliance with the entity or the subject matter.

Identifying control risks (CR)

Control risk is the risk that the relevant internal controls associated with the inherent risks are inappropriate or do not work properly. As a result, the entity will fail to prevent material non-compliances or detect and correct them on a timely basis. The auditor assesses the control risks based on the understanding and evaluation of the entity's internal control system.

Auditors would ask questions about controls structured around the five components (i.e., control activities, risk assessment, information and communication, monitoring, and control environment) of the internal control system. The auditor's primary consideration is whether, and how, a specific control prevents, detects and corrects a non-compliance. If an expected control does not exist, the auditor enquires whether any compensating controls are in place that would have the same effect as the original control.

Walk-through tests: To determine the proper functioning of control, the auditor carries out 'walk-through tests' of a small number of transactions (if the audit's subject matter is budget execution or expenditure) or the operations of the entity under audit. Note that obtaining an understanding of an entity's controls should not be considered to be a test of its operating effectiveness; such testing is carried out in the audit conducting phase.

Focus on relevant controls: The auditor considers only those controls that are relevant to the audit objective. It is a matter for the auditor's professional judgment as to whether a control, individually or in combination with others, is relevant to the inherent risks of the subject matter. Furthermore, the auditor determines which controls are to be considered key. The auditor selects an appropriate number of key controls for testing to ensure that all relevant risks are covered. While choosing the controls, the auditor may consider the following:

→ Significance of the related risk (materiality)	→ Applicable legal and regulatory requirements
→ Nature of the entity's business, including its organisation	→ Circumstances and the applicable component of internal control
→ Diversity and complexity of the entity's operations	→ Nature and complexity of the systems that are part of the entity's internal control
→ Size of the entity	→ Whether, and how, a specific control prevents, or detects and corrects non-compliance

There is a direct relationship between the entity's objectives, which the entity strives to achieve, and the internal control components that enable it to achieve the objectives. All internal control components are relevant to each category of entity objectives. When looking at any one category – the effectiveness and efficiency of operations, for instance – all five components of internal control must be present and functioning effectively to conclude that internal control over the entity's operations is effective.

The detection risk (DR)

Detection risk is under the auditor's control. It is the risk that the auditor will not be able to detect non-compliance that has not been corrected by the organisation's internal controls. ISSAI 4000.52 states, 'The auditor shall perform procedures to reduce the risk of producing incorrect conclusions to an acceptable low level.' Reducing audit risk includes[56]:

- Anticipating the possible or known risks of the work envisaged and the consequences thereof, and
- Developing procedures to address those risks during the audit and documenting which and how those risks will be addressed.

The auditor can reduce detection risk by auditing the subject matter in a planned and structured manner and by identifying the inherent and control risks to the greatest extent possible. In the audit assurance model, 95% confidence is required through substantive procedures or in combination with tests of controls. The assurance level of 95% corresponds to an audit risk of 5%.

The auditor designs appropriate audit procedures to reduce the detection risks to an appropriately low level; it is recommended to keep the overall audit risk at 5%. Detection risk, however, can only be reduced, not eliminated, because of the inherent limitations of an audit. Accordingly, some detection risk will always exist.

To enhance the effectiveness of an audit procedure and its application, and to reduce the possibility that the auditor might select an inappropriate audit procedure or misinterpret the audit results, it is essential to ensure:

- Adequate risk assessment in the planning phase
- Assignment of competent personnel to the engagement team
- That the auditor exercises professional scepticism
- Supervision and review of the audit work performed

The following table shows the components of the audit risk and the resulting assurance that can be derived from the control test and substantive procedures.

Assessed inherent risk	Evaluation of the entity's internal control system	Assurance from the combined risk assessment	Confidence from inherent and control assurance	Substantive testing to be carried out
Low	Adequate	High control assurance	Both inherent assurance and control assurance	Minimum
	Not adequate	No control assurance	Inherent assurance, but no control assurance	Standard
High	Adequate	High control assurance	No inherent assurance, but control assurance; control test can be extended to reduce substantive test	Standard
	Not adequate	No control assurance	No inherent assurance, and no control assurance; assurance only from the substantive test	Maximum and focused

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[56] ISSAI 4000.53

Auditors use this table to determine and develop the audit approach. It demonstrates that the extent of the audit work is based on perceived risks and the effectiveness of controls to mitigate them. In the case of an audit where the inherent risk is high, and the internal control is not adequate, the auditor develops the plan considering no inherent and control assurance. The auditor will perform a focused audit, applying professional judgment and conducting maximum substantive procedures, as explained in Chapter 6.

Identifying fraud risk

ISSAI 4000.58 states, 'The auditor shall consider the risk of fraud throughout the audit process, and document the result of the assessment.' While detecting potential unlawful acts, including fraud, is usually not the main objective of the compliance audit, 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.

Auditors looking for material fraud risks should exercise professional scepticism, discuss the issues with management, apply the audit tests unpredictably and follow up on management override of controls. Auditors also analyse the elements generally present in a fraud. The elements are presented in what is commonly referred to as the fraud triangle:

- Incentive or pressure to commit fraud
- Opportunity to commit the fraud
- An attitude or rationalisation to justify the fraud

FIGURE 5.3
The fraud triangle

Opportunity

Fraud

Pressure

Rationalisation
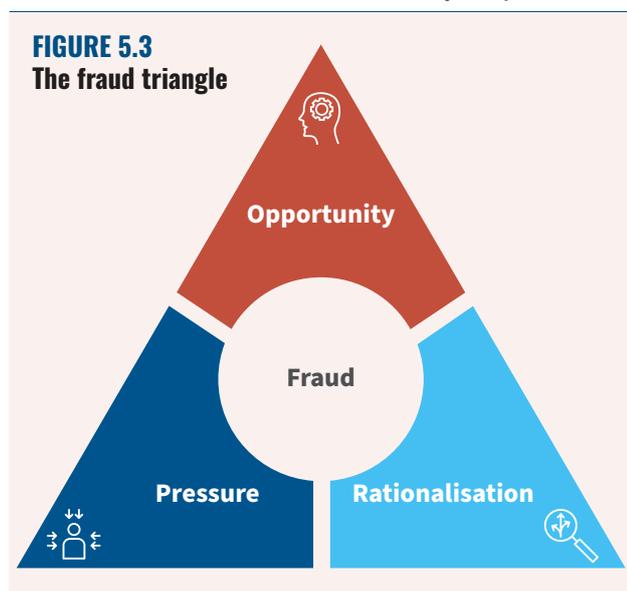
The opportunity to commit fraud generally arises from inadequate, ineffective or missing internal controls. Auditors should use their professional judgment in assessing the risk of non-compliance due to fraud according to four risk attributes:

- Type of risk involved
- Significance of the risk (materiality)
- Likelihood of the risk causing a material non-compliance
- The pervasiveness of the risk

Auditors should be alert to the possibility of fraud and set risk-based priorities for their tests to detect the different types of deliberate non-compliance possible and to report on fraudulent financial reporting, misappropriation of assets and corruption. SAIs with sufficient resources may establish a risk assessment team which can provide input on fraud risks to the audit team.

If suspicion of unlawful acts arises during the audit, the auditor may communicate this to the appropriate levels of management and those charged with governance. Those charged with governance are likely to be administrative bodies higher up in the reporting hierarchy. Where relevant and reasonable, the auditor may 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. The auditor may also report such incidents directly to the relevant law enforcement authorities.[57]

Note: Because of the different mandates and organisational structures that exist internationally, it is up to the SAI to determine the appropriate action to take regarding instances of non-compliance related to fraud or serious irregularities.[58] The auditors take action to ensure that they respond appropriately in accordance with the SAI's mandate and the particular circumstances.

The audit team can document the fraud risks with the suggested working paper template provided in **Exhibit 5.4**.

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[57] ISSAI 4000.231

[58] ISSAI 400

ISSAI 4000.55 states that, in a direct reporting engagement, 'The auditor may apply the audit risk model in forming a conclusion on the subject matter.' The auditor can follow an abridged process. By identifying and assessing the entity's inherent and control risks, the auditor can define the nature and extent of the evidence-gathering procedures required to test compliance with the criteria. The higher the level of risk, the greater the extent of audit work required to lower detection risk sufficiently to achieve the acceptable level of audit risk.[59]

The risk identification and assessment process for planning a direct reporting engagement may consist of the four steps in Figure 5.4.[60]

The process allows the auditor to start with the acquired knowledge of the subject matter and to eventually focus on the critical risks that lead to the relevant audit questions. The auditor can apply the process of identifying inherent and control risks in step 1, following the stages of understanding the entity and the internal control, as explained above.

FIGURE 5.4:
Risk assessment process for a direct reporting engagement

STEP 1 — **Document the subject matter in a flow-diagram with the key controls**
- Achieve an understanding of the entity and its internal control
- Consider risks, controls

Flowcharts Templates

STEP 2 — **Identify the risks**
- List possible risks
- Identify main risks to assess

Identified risks

STEP 3 — **Analyse the risk to assess risk level**
- Analyse main risks
- Risk level
- Likelihood and impact

Analysed risks

STEP 4 — **Focus the key risk to define the question and procedures**
- Questions to address risks
- Consider criteria
- Procedures to perform

To risks register for designing audit procedures

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[59] ISSAI 4000.56

[60] https://www.eca.europa.eu/Lists/ECADocuments/GUIDELINE_RISK_102013/GUIDELINE_RISK_102013_EN.pdf

Assessment of the risks

The auditor assesses all risks identified in the previous steps. As part of the risk assessment, the auditor determines which of the inherent risks identified, in his/her judgment, require special audit consideration (significant risks), which are derived from business or operational risks that may result in non-compliance. The auditor should evaluate the design of the related controls and determine through testing whether these controls have been implemented effectively and continuously throughout the period under review.

For example, if the subject matter of an audit is the expenditure of the entity, the auditor considers whether the risk:

- Involves significant transactions;
- Involves significant non-routine transactions that are outside the normal course of operation for the entity or that appear to be unusual;
- Is a risk of fraud; and
- Is related to any recent developments and therefore requires specific attention.

The auditor considers the complexity of transactions and the degree of subjectivity in the measurement of financial information related to the risks.

The assessment of risks, based on the determination of significant risks, is a matter for the auditor's professional judgment. To determine whether the risk warrants audit consideration, the auditor examines the nature of the risk, the likely impact of potential non-compliance and the likelihood of the risk materialising.

Determining the likelihood of risks materialising is a fundamental challenge in the risk assessment process. The auditor will work based on assumptions, and these assumptions should be reasonable and documented.

The auditor then has to determine the likely impacts or consequences on the organisation and the achievement of relevant objectives, if the risk should materialise.

Example:

The auditor may determine a level – high, medium or low – of occurrence (likelihood) and seriousness (impact) for each risk using the risk matrix below. The overall evaluation of the risks is the result of the combination of both elements.[61]

Likelihood	Impact		
	Low	Medium	High
Low			
Medium			
High			

Overall risk evaluation:	Low_____ Risk can be ignored	Medium_____ Judgment based on the characteristics of the risk	High _____ Risk must be followed up by the audit

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[61] https://www.eca.europa.eu/Lists/ECADocuments/GUIDELINE_RISK_102013/GUIDELINE_RISK_102013_EN.pdf

An illustration of the risk assessment in planning is provided below.

	Example: Risk assessment of the operations of a city council
Background	The subject matter of the audit is 'the operations of a city council', responsible for city governance. The council has various operations, e.g. land management, building management, licensing, revenue collection and tax collection. It also has the budget execution and expenditure aspect of its operations. The auditor scoped the audit on the activities and services of the city council, specifically the land management and building management and how the entity is complying with the applicable criteria in accomplishing the two functions.
Risk assessment	The auditor identifies risks using the process described in section 5.2, by assessing the inherent and control risks. The risks are identified by analysing the process flow of each function – building management and land management – while understanding the entity and its control environment. The audit team has assessed the risks and documented the significant risks in the risk register. Only the identified were included in the risk register, and the audit procedures were designed accordingly. During the audit, the team identified additional risks for both the land and building management. The team documented the new risks and modified the audit plan accordingly. If the audit's subject matter is the council's expenditure and budget execution, the auditor can perform the risk assessment considering all operations related to the expenditure.

Determine materiality

ISSAI 4000.125 states, 'The auditor shall determine materiality to form a basis for the design of the audit, and re-assess it throughout the audit process.' After selecting the significant audit areas, the auditor determines materiality.[62] The auditor then selects the subject matter and criteria, taking into consideration the risk and materiality.[63]

While planning the audit, the auditor chooses the materiality based on the needs of the intended user(s).[64] Determining materiality is a matter of professional judgment and depends on the auditor's interpretation of the users' needs. The intended user may judge a matter material if information about it is likely to influence the user's decision-making process.

Assessing materiality in planning phase	• Helps the auditor to identify the audit questions which are of importance to the intended user(s). • Helps assess the material risks and determine the nature, timing and extent of audit procedures (*ISSAI 4000.70*).
Assessing materiality in conducting phase	• The auditor uses materiality in deciding the extent of audit procedures to be executed and in the evaluation of audit evidence. • In evaluating evidence and concluding the audit, the auditor uses materiality to evaluate the scope of work and the level of non-compliance to determine the impact on the conclusion or opinion.
Assessing materiality in reporting	• In a direct reporting - reasonable assurance engagement, 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 (*ISSAI 4000.38*).

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[62] ISSAI 4000.128

[63] ISSAI 4000.37

[64] ISSAI 4000.103

ISSAI 4000.127 states, 'Materiality may focus on quantitative factors such as the number of persons or entities affected by the particular subject matter or the monetary amounts involved as well as the misuse of public funds, regardless of the amount.'

Quantitative materiality: ISSAI 4000.129 states, 'Quantitative materiality is determined by applying a percentage to a chosen benchmark as a starting point… This involves the exercise of professional judgment and reflects, in the auditor's judgment, the measures that user(s) of the information are most likely to consider important.'

ISSAI 4000.186 states that materiality by value can involve, based on the subject matter, amounts (monetary amounts) or other quantitative measures such as the number of citizens or entities involved, carbon emission levels and delays in meeting deadlines.

The auditor can apply the threshold percentage between 0.5% and 5% for quantitative materiality. This choice is a matter of judgment, based on the auditor's assessment of internal control, risk assessment, the sensitivity of the subject matter and the needs of the intended users. The auditor can apply a different threshold percentage considering the users' needs. In addition to the threshold percentage, a ceiling may also be set in terms of the absolute amount.

Quantitative materiality is primarily used in attestation engagement. When performing such engagements, the auditor might want to select separate levels of materiality for classes of transactions or balances that are more important to the account user(s) or that have a higher risk of non-compliance material by nature or context. In a direct reporting engagement, when the subject matter is the expenditure of an entity, the auditor may apply quantitative materiality.

ILLUSTRATION 5.3:
Determining quantitative materiality

Example: Calculation of overall quantitative materiality	
Determining quantitative materiality requires the auditor to identify the materiality base and the percentage to apply to the gross amount. The percentage is determined based on the status of risks and controls, the sensitivity of the subject matter and user needs. In this example, the auditor is using 1.5%, considering that the subject matter is relatively sensitive.	
	Sensitivity of the subject matter 0.5% --------> 5%
Materiality base	Materiality threshold – 1.5%
Gross expenditure amount	345,000,000
Materiality level	345,000,000 x 1.5% = 5,175,000

The quantitative materiality level is 5,175,000. This means that if the value of non-compliance exceeds this limit, it can be considered material and would affect the audit conclusion. Auditors should consider the pervasiveness of the non-compliance.

The level of materiality will influence the amount of audit work the auditor undertakes. The percentage ranges to be used are set by the audit team, depending on the materiality basis adopted. The choice of percentage should be based on the risk profile and characteristics of the subject matter being audited, i.e., the level of public and parliamentary interest in it, particularly if the audit report will be used to hold the responsible party accountable.

Because the risk profiles, the sensitivity of the transactions and the effectiveness of internal controls may differ across the subject matters, the materiality threshold may also be set differently. The auditor may consider setting up materiality thresholds separately from the overall materiality. This can be done by applying the overall threshold percentage used to determine the overall materiality level to the population value of that particular area of the subject matter. Or, if the risk profiles, sensitivity and effectiveness of internal control vary significantly, the auditor may apply an appropriate threshold percentage to reflect that.

In a compliance audit, there may be situations in which quantitative materiality does not apply to a particular subject matter. Hence, the qualitative aspects of materiality become more pertinent.

Qualitative materiality: ISSAI 4000.130 states, 'In some cases, the qualitative factors are more important than the quantitative factors. Public expectations and public interest are examples of qualitative factors that may impact the auditor's determination of materiality.'

The relative importance of qualitative factors when considering materiality in a particular audit is a matter of the auditor's professional judgment. The qualitative factors may include:

- The relationship between various parts of the subject matter if non-compliance in one area of the subject matter affects the others
- The nature of observed non-compliance with a control when the subject matter information is a statement that the control is effective
- Whether non-compliance is the result of an intentional or unintentional act
- When the subject matter is a government programme or an entity, whether a particular aspect of the programme or entity is significant with regard to the nature, visibility and sensitivity of the programme or entity
- When the subject matter information relates to a conclusion on compliance with law or regulation, the seriousness of the consequences of non-compliance

The scenario below illustrates the aspects of qualitative materiality.

Example: Consideration of qualitative materiality
The terms of a building code require the building inspector to perform several annual inspections. The government agency has not performed inspections for the past five years. This non-compliance may be significant due to qualitative aspects such as safety implications. Although no monetary amounts are involved, the non-compliance may be considered material due to the potential consequences it may have on the safety of building occupants. Moreover, in the event of a disaster, there is a risk that non-compliance may result in significant liability claims, which could have material financial implications for the government agency.

As stated in ISSAI 4000.127, the inherent nature or characteristics of an item or group of items may also render a matter material (qualitative materiality). Qualitative materiality is determined by the nature and context of the subject matter.

Material by nature is related to inherent characteristics and concerns issues where there may be specific disclosure requirements or high political or public interest. It includes any suspicion of serious mismanagement, fraud, illegality, irregularity or intentional misstatement or misrepresentation of results or information. Materiality, by nature, may arise due to non-compliance:

- Of high officials who raise suspicion involving conflicts of interest
- That may suggest fraudulent activity or corruption
- In an area where there is a high degree of public interest
- Where the legislation or regulations make clear that it is a serious offence, regardless of the monetary value

Material by context concerns items that are material by their circumstance, so that they change the impression given to the users. It includes instances in which a minor error or non-compliance may have a significant effect, e.g., misclassification of expenditure as income so that an actual deficit is reported as a surplus.

For example, where the total value of non-compliance is below the materiality threshold, but the auditor is aware that a stakeholder, such as Parliament, has expressed a special interest in the apparent irregularities in the subject matter, the auditor thus considers the issue material, even though its value is not material.

Setting a qualitative threshold is sometimes advisable when a quantitative materiality threshold cannot be established, because non-compliance cannot always be quantified in terms of amounts or monetary values. It could be more appropriate for the audit team to set a tolerable rate of non-compliance as a threshold for the subject matter as a whole and, where applicable, for different areas of the subject matter. However, the auditor should also define what constitutes a material non-compliance, as non-compliance with varying levels of authorities, such as parliamentary legislation, regulations, or guidelines, will differ in their hierarchy and significance.

If the subject matter is sensitive and there is high interest from the Parliament, the public, and the media, a lower tolerable non-compliance rate would entail more audit tests and greater assurance on the areas assessed.

ISSAI 4000.92 states that, at the audit planning stage, the auditor's documentation should include an assessment of the materiality of the subject matter. The auditor can document the evaluation of materiality at the planning stage with the working paper template in Exhibit 5.5.

Result of risk assessment: Risk register

Once the auditor identifies and assesses all risks and determines the material risks, they are listed in a risk register and considered for audit testing. This listing is to document all potential risks of non-compliance in a step-by-step, systematic process. The audit team may consider other appropriate forms of documentation of the risks. From the risk register, the audit team may further elaborate on the risks using a suggestive tool – the audit planning matrix – which identifies the appropriate audit procedures to be performed and the evidence to be collected. The audit team can document the risks identified for the audit with the suggested working paper template provided in **Exhibit 5.6**.

Design audit procedures to respond to the assessed risks

ISSAI 4000.149 states that the auditor needs to plan appropriate responses to assessed risks (identified and documented in the risk register). Responses to the assessed risks include designing audit procedures to address them.

The nature, timing and extent of the audit procedures to be performed may vary from one audit to another. Nonetheless, compliance audit procedures, in general, involve establishing the relevant criteria, i.e., the authorities that govern the entity, and then measuring the relevant subject matter against those authorities.

The auditor can use an audit planning matrix (shown in Illustration 5.4) for documenting the responses to the assessed risks. The matrix provides a structure for the essential design components and makes planning systematic and directed. The aim is to facilitate communication of the decisions on the methodology and assist with the fieldwork. The matrix outlines the requirements and procedures necessary to implement the audit objective and to assess each identified risk against the audit criteria in the risk register.

The matrix is flexible, and the team should update or modify it as the audit progresses. It establishes a relationship between the audit objectives, audit procedures, and the audit fieldwork. It also facilitates audit supervision and quality review.

Audit procedures include substantive procedures and tests of controls. Substantive procedures include both tests of details and analytical procedures. Suppose auditors intend to rely on the operating effectiveness of controls. In that case, they need to obtain evidence that the controls are operating effectively when determining the nature, timing and extent of substantive procedures. The design and implementation of key controls relevant to the subject matter might be evaluated as adequate.

The audit team can document the audit procedures to be performed in the matrix using the suggested working paper template provided in **Exhibit 5.7**. Based on the designed audit procedures for the identified risks and the potential audit evidence to be collected during the audit, the auditors perform the audit, which is explained in Chapter 6.

LLUSTRATION 5.4:
Audit planning matrix

No.	1 Risks identified (from the risk register Exhibit 5.6)	2 Criteria	3 Required evidence or information	4 Source of evidence or information	5 Audit procedures to perform
1.	Risk 1				
2.	Risk 2				
3.	…				

5.3 DOCUMENTING AND ENSURING THE QUALITY OF THE AUDIT STRATEGY AND AUDIT PLAN

Documenting the audit strategy and the audit plan is the final step of the planning process. By this point, the audit team has examined all critical aspects of the audit. Team members have reached an understanding on what they will do in the audit (documented in the audit strategy) and how they will do it (documented in the audit plan).

Planning also involves considerations regarding the direction, supervision, and review of the audit team and its work. The auditor can prepare both the audit strategy and the audit plan as a single document for approval by SAI management before commencing audit fieldwork. In the process, the auditor should review the audit plan and strategy and address the significant matter(s) raised during the review, revision, finalisation and sign-off of the strategy and plan by the management.

All exhibits provided in this chapter will serve as input to the development of the audit plan document. The interlinkages between the exhibits and their output can be shown as in Illustration 5.5.

Exhibits 5.2 to 5.5 identify the risks relevant to the audit. The audit procedures and audit evidence to be collected are documented in Exhibit 5.7, along with the matrix. The auditor updates both the audit strategy and the audit plan as necessary throughout the audit process.

The audit plan should be reviewed, modified if necessary and approved by the appropriate official who has supervisory authority over the audit team. Suppose the SAI structure lacks such a supervisory layer. In that case, the plan should be reviewed by another auditor of adequate seniority and authority within the SAI who has successfully performed audits of a similar type and complexity, and who is independent of the audit team. All such reviews and any approvals should be documented. Those responsible for reviewing the audit plan may consider the suggestive quality checklist provided in **Appendix 5-A**.

ILLUSTRATION 5.5:
Documenting the audit plan

EXHIBIT 5.1 — Audit Strategy

EXHIBIT 5.2 — Understand entity

Inherent risks

EXHIBIT 5.5 — Materiality

EXHIBIT 5.3 — Internal control

Control risks

EXHIBIT 5.5 — Materiality

EXHIBIT 5.6 — Risk register

EXHIBIT 5.7 — Audit plan

EXHIBIT 5.4 — Fraud risk

EXHIBIT 5.5 — Materiality

Audit strategy and audit plan
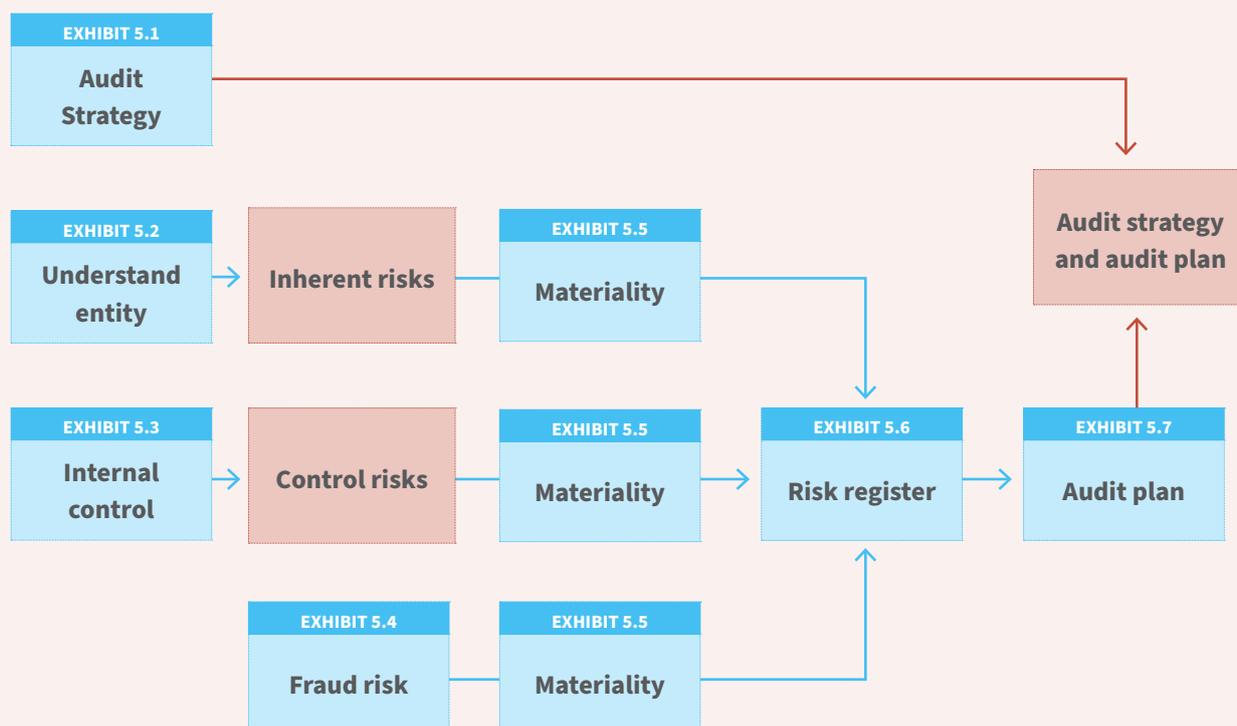
PERFORMING AUDIT PROCEDURES, GATHERING AND EVALUATING EVIDENCE

During the audit fieldwork phase, auditors perform the audit procedures for the risks identified in the audit plan. In this phase, the auditors select samples, if required, from the subject matter, gather evidence and evaluate the audit evidence. This chapter begins with the types and characteristics of sufficient and appropriate audit evidence. It then describes the appropriate sampling method for the specific type of engagement. It explains the various evidence-gathering techniques and how the auditor can evaluate the evidence gathered to form the conclusion for a direct reporting engagement.

6.1 AUDIT EVIDENCE

Audit evidence is the information on which the auditor's conclusion or opinion is based. Auditors design and apply the necessary audit procedures to obtain sufficient and appropriate audit evidence to form a conclusion or opinion on whether the subject matter complies, in all material respects, with the established criteria.

To cover the audit scope, the auditor has to decide when the audit evidence is sufficient and appropriate to provide a basis for a conclusion or an opinion. In the planning phase, auditors review the:

- Internal controls established by the audited entity to prevent, detect and rectify instances of non-compliance, and
- 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 take these into consideration while they begin gathering audit evidence. The following are the different types of evidence.

Testimonial evidence

This evidence is what the audited entity's staff tell the auditor. Although it is the weakest form of evidence, some testimonial evidence is more substantial than others. For example, the staff who perform the task can better explain how the task is actually performed than the supervisor, who is aware of how it should be performed. Testimonial evidence from two or more people is stronger than it is from one person.

Documentary evidence

This type of evidence is contained in the documents. It is the second-strongest type of evidence; however, it is important to consider the source of the document. Records produced by the entity's information systems are a common form of evidence auditors use. Documents from external sources are stronger than internal documents; however, they are not as strong as the documents sent directly to the auditors. For example, an entity employee might produce a fictitious invoice from a non-existent vendor.

Physical evidence

This type of evidence is what auditors observe during an audit. The most common is the evidence auditors see during an inventory count or when observing the areas where an entity releases toxic chemicals. This is considered the strongest form of evidence. The auditor needs to consider what the evidence proves and what it does not prove.

Analytical evidence

The auditor obtains this type of evidence by comparing, computing, or otherwise analysing the data. Auditors can review the budget-to-actual expenditure comparisons. Analytical evidence indicates that certain relationships exist among the analysed data. The auditor usually investigates further to identify the causes of such relationships.

Circumstantial evidence

This is not direct evidence but is related to the circumstances. In this case, the auditor presents evidence of other facts that, based on a reasonable inference, would lead the auditor to believe the intended fact to be proved. In other words, circumstantial evidence means all proof other than direct proof of non-compliance. Usually, this evidence is used in ascertaining non-compliance due to fraud. For example, in a potential fraud or corruption scenario, it is evidence of the standard behaviour, the employee's breach and the irregular payments.

6.2 SUFFICIENT AND APPROPRIATE AUDIT EVIDENCE

Sufficiency and appropriateness are interrelated. The auditor exercises professional judgment and scepticism when assessing the quantity (sufficiency) and quality (appropriateness) of the evidence while determining the nature, timing and extent of the audit procedures to be performed.

The auditor will often need to combine and compare evidence from different sources to meet the requirements for sufficiency and appropriateness of audit evidence. The nature and sources of necessary audit evidence are determined by the following:

Subject matter	Audit scope	Criteria
	Level of assurance	Materiality	

Sufficiency of audit evidence: Quantity

Sufficiency is the quantity of evidence required to support the audit findings and conclusions. There is no formula to express in absolute terms how much evidence there must be to be considered sufficient. In assessing the sufficiency of the evidence, the auditor needs to determine whether enough evidence has been obtained to persuade a knowledgeable person that the findings are reasonable.[65]

The quantity of audit evidence required depends on the nature of the audit task. For example, in a reasonable assurance engagement, the auditor needs to obtain more evidence than in a limited assurance engagement to form a conclusion.[66] Also, a broader audit scope requires more audit evidence than a narrower scope.

The quantity of evidence depends on audit risk. The higher the risk, the more evidence is likely to be required. For the quality of evidence, the higher the quality, the less evidence may be required.[67] However, simply gathering more evidence does not compensate for poor quality.[68]

What constitutes the evidence as sufficient and appropriate is the auditor's professional judgment, and it is influenced by the following:

AUDITOR'S JUDGMENT ON THE EVIDENCE IS BASED ON THE:

- Significance of a potential non-compliance
- Likelihood of non-compliance having a material effect on the subject matter
- Effectiveness of the responses by the entity to address risk of non-compliance
- Experience from previous audits with similar non-compliance
- Results of the audit procedures performed
- Source and reliability of the available information
- Persuasiveness of the evidence
- Understanding of the responsible party and its environment

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[65] ISSAI 4000.147

[66] ISSAI 4000.146

[67] ISSAI 4000.151

[68] ISSAI 4000.152

Appropriateness of audit evidence: Quality

Appropriateness is a measure of the quality of the audit evidence. It includes relevance, validity and reliability.[69]

RELEVANCE

→ The extent to which evidence has a logical relationship with and importance to the issue being addressed.

→ Evidence helps to answer the audit objective.

→ Evidence applies to the period under review.

VALIDITY

→ The extent to which the evidence is a meaningful or a reasonable basis for measuring what is being evaluated.

→ Evidence represents what it is purported to represent.

RELIABILITY

→ The extent to which the audit evidence has been gathered and produced following a transparent method.

→ Evidence fulfils the requirements for credibility.

→ The reliability of evidence is affected by its source (internal or external), type (physical, documentary, oral or analytical) and the circumstances.

While recognising that exceptions may exist, audit evidence is more reliable when it is:

Obtained from independent sources	From outside the entity, e.g., confirmation received from a third party, rather than generated internally.
Subject to effective related controls	Internally generated
Obtained directly by the auditor	For example, direct observation of the application of control, rather than indirect enquiry about the implementation of a control
In documentary form	Whether paper, electronic or another medium, rather than verbal statements
Provided in the original documents	Rather than photocopy

Other considerations on audit evidence

Auditors should adequately document the audit evidence in the working papers. Such documentation includes the work performed, findings and conclusions, and the rationale for significant decisions. Information that is not pertinent to work done or conclusions reached should not be included. Auditors also consider:

CORROBORATING THE EVIDENCE
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.

PERFORMING ADDITIONAL PROCEDURES
In cases where evidence obtained from one source is inconsistent with that obtained from another, the auditor needs to determine what additional procedures are needed to resolve the inconsistency.

USE OF CONFIDENTIAL EVIDENCE
If documents produced by management are classified as confidential, the auditor or his/her superior at the appropriate level will discuss how this confidential information might best be used.

EVIDENCE ON FRAUD
Information and documentation relating to cases of discovered or suspected fraud should be handled with particular care.

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[69] ISSAI 4000.148

6.3 EVIDENCE-GATHERING TECHNIQUES

ISSAI 4000.144 states, 'The auditor shall plan and perform procedures to obtain sufficient and appropriate audit evidence to form a conclusion with the selected level of assurance.' Obtaining sufficient and appropriate audit evidence is a systematic and iterative process as it involves the following:
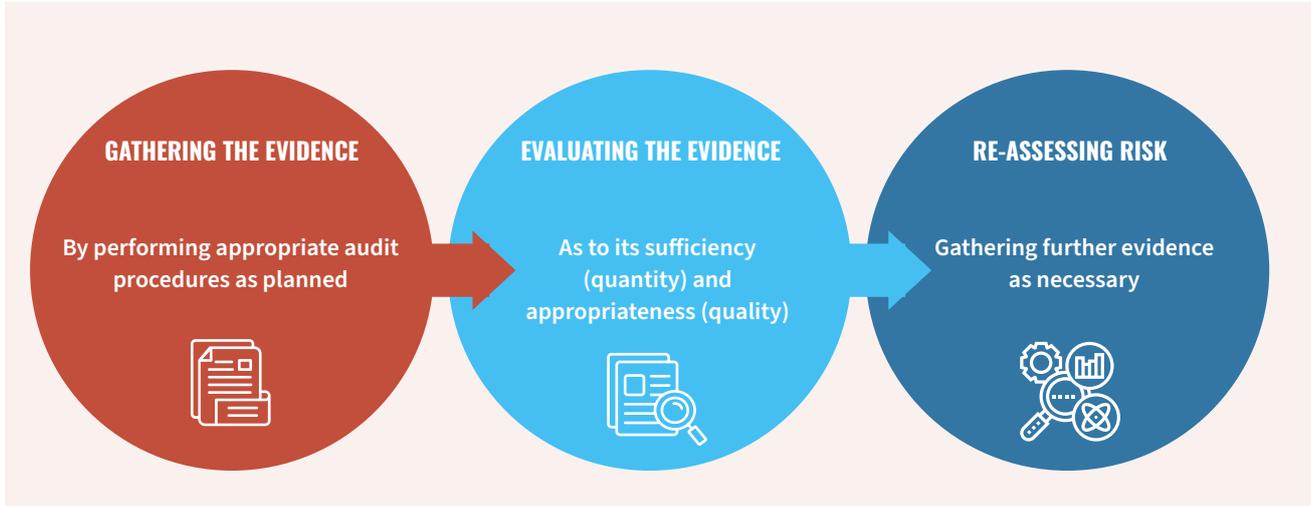
As the auditor performs planned audit procedures, the audit evidence obtained may lead the auditor to modify the nature, timing or extent of other planned audit procedures. Information may come to the auditor's attention that differs significantly from the information on which the risk assessments were based at the outset.

For example, the extent of non-compliance detected through audit procedures may alter the auditor's judgment of 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 a revised consideration of assessed risks.

ISSAI 4000.158 states, 'The auditor shall select a combination of audit techniques to be able to form a conclusion with the selected level of assurance.'

Evidence may be obtained through a variety of techniques. The auditor should make a judgment as to which method (or a combination thereof) for obtaining audit evidence will be suitably reliable and should balance the reliability of the evidence against the cost of getting it. Commonly used evidence-gathering techniques are[70] the test of controls (observation, inspection, inquiry, re-performance) and substantive procedures (test of details and analytical procedures).

Test of controls

The test of controls involves evaluating the controls management has put in place to reduce the risk of non-compliance or the risk that the subject matter information is materially misstated. For most subject matters, testing key controls is an effective way to collect audit evidence.[71]

The auditor performs tests of controls to confirm the preliminary assessment of those key controls upon which s/he intends to rely. The objective of tests of controls is to evaluate whether the key controls operated effectively and continuously during the period under review.

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[70] ISSAI 4000.160

[71] ISSAI 4000.168

- If the tests of controls confirm that the controls have operated continuously and effectively throughout the period under review, then reliance can be placed on these controls, and minimum substantive testing can be performed. When these controls are found not to have operated continuously and effectively throughout the period under review, the auditor should reassess the audit approach and increase the extent of substantive testing to be performed.

- The techniques that are generally used to test key controls are observation and enquiry, inspection and re-calculation, or a combination thereof. The auditor can document testing the operating effectiveness of controls using the working paper template provided in **Exhibit 6.1.**

Observation involves looking at a process or procedure being performed by others. Observation provides audit evidence of the performance of a method or system, but is limited to the point in time at which the observation occurs, and to the fact that being observed may affect how the process or procedure is performed.[72] In performing a compliance audit, this may, for example, include looking at how a bid tendering process is carried out or observing how benefit payments are processed in practice.

The inspection involves examining books, records, or documents, whether internal or external, in paper, electronic, or physical form. The auditor considers the reliability of any documents inspected and remains conscious of the risk of fraud and the possibility that papers examined may not be authentic.[73] In performing a compliance audit, the inspection may, for example, include reviewing case files or other relevant documents to determine whether recipients of benefits met eligibility requirements, or examining an asset, such as a bridge or a building, to determine if it meets the applicable building specifications.

Inquiry involves seeking information from relevant persons, both within and outside the audited entity. Depending on the subject matter and the scope, interviews and questionnaires alone will, in most cases, not be sufficient and appropriate evidence. Other relevant evidence-gathering methods to be considered include written documentation from the audited entity.[74] The 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 within a country or state, inquiries could be made of officers as to how relevant legislation, including changes and updates, is identified and interpreted.

SAIs with jurisdictional powers may use the method of inquiry as set out in the laws governing the auditing procedures. An inquiry may involve preparing and sending a written communication to the relevant responsible persons, asking for specific information that the audit team considers necessary to support the conclusions.[75]

External confirmation is audit evidence obtained by the auditor in the form of a direct written response from a third party. The auditor is getting feedback directly from the beneficiaries or third parties who have received the grants. The audited entity asserts that it has been paid, or confirms that funds have been used for the purpose set out in a grant or funding agreement.[76]

Re-performance involves independently carrying out the same procedures already performed by the audited entity, including controls initially performed as part of the entity's internal control. Re-performance may be done manually or by computer-assisted audit techniques. Where highly technical matters are involved, external experts may be needed.[77]

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[72] ISSAI 4000.161

[73] ISSAI 4000.162

[74] ISSAI 4000.163

[75] ISSAI 4000.171

[76] ISSAI 4000.164

[77] ISSAI 4000.165

Re-calculation consists of checking the mathematical accuracy of documents or records. Re-calculation may be performed manually or electronically.[78] Some examples of re-performance are:

- Review of individual case files to test whether the audited entity made the correct decisions or provided the appropriate service in accordance with the relevant criteria
- Re-performance of process steps to test the appropriateness of visas or residence permits issued
- Re-computation of taxation deductions on audited entity staff payroll to confirm the correct amounts payable in taxes

Substantive procedures

Substantive procedures include tests of details and analytical procedures.

Tests of details involve testing detailed transactions or activities against the audit criteria. Substantive testing must always be included in attestation engagements.[79] In most direct reporting engagements, auditors conduct substantive testing. This is because, at the planning stage, while identifying risks, auditors determined that there are very limited or non-existent internal controls within the entity. Depending on how well the entity has managed the subject matter, the auditor may decide not to test and evaluate internal controls separately but rather examine relevant controls alongside substantive testing.

The substantive procedures were designed during the planning phase to be responsive to the related risk assessment; their purpose is to obtain audit evidence to detect non-compliance. However, irrespective of the assessed risk and level of reliance, the auditor should design and perform substantive procedures (tests of details) for each material area. Substantive testing typically includes the following:

ILLUSTRATION 6.1:

Substantive procedures

Substantive test	Areas
Computation	→ Re-performance of calculations of claims, grants
Analysis (excluding analytical review)	→ Analysis of findings of work by internal and other auditors → Analysis of legal basis, legal and budgetary commitments, eligibility, and tendering procedures
Re-performance	→ Re-performance of already inspected or audited transactions
Inspection	→ Physical assets → Contracts → Claims → Ex-ante and ex-post control reports → Audit reports (internal and external) → Monitoring reports → Supporting documents, e.g., invoices, public procurement documents, cost–benefit analysis, photos, records of beneficiaries
Inquiry and confirmation	→ Inquiry of auditee management and staff → Circularisation of bank balances → Circularisation of receivables
Observation	→ On-the-spot checks

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[78] ISSAI 4000.166

[79] ISSAI 4000.167

The auditor should carry out substantive tests as designed in the planning phase unless the evaluation of the results of tests of controls requires him/her to reconsider the nature, timing and extent of the tests of details. The auditor can document the substantive testing procedures using the working paper template provided in **Exhibit 6.2.**

Analytical procedures involve acquiring information from various sources to determine expectations, comparing the actual situation with those expectations, investigating the reasons for any discrepancies arising and evaluating the results. These procedures can be used both as part of the risk analysis and when collecting audit evidence. Audit evidence can be obtained either by comparing data and investigating fluctuations, or by identifying relationships that appear inconsistent with expectations based on historical data or the auditor's experience. Regression analysis techniques or other mathematical methods may assist public sector auditors in comparing actual with expected results.

In a limited assurance engagement, analytical procedures and inspections are usually sufficient to form a conclusion with limited assurance. In contrast, a conclusion with reasonable assurance must be formed from a combination of audit techniques.[80]

However, in a compliance audit, analytical procedures may, only in certain circumstances, assist the auditor in evaluating compliance. For example, where allowances under a grants scheme are subject to a maximum value and the number of recipients is known, the auditor may use analytical procedures to establish whether the permitted maximum has been breached. These techniques or combinations thereof may be used for tests of controls or substantive procedures.

Considerations in gathering evidence

The auditor may consider the reliability of the evidence as a general guideline, but it may vary across entities. The following is the hierarchy of the reliability of the types of evidence[81]:

Level of reliability	Types of evidence
High	→ Physical examination → Re-performance
Medium	→ Documentation → Confirmation → Analytical procedures
Low	→ Inquiries of entity personnel or management → Observation

In some situations, the auditor may consider confirmations as a highly reliable source of evidence when an independent third party is qualified to respond to the auditor's request. So, the level of reliability is subject to a number of exceptions considering the audit context.

The auditor may use one or more of these procedures based on the risks of non-compliance with the criteria and other information under audit. The following table[82] shows the types of evidence and the relevant audit procedures to gather evidence.

Types of evidence	Evidence-gathering procedures
Auditor's calculations	→ Recalculation by the auditor
Physical observation, inspection	→ Observation and examination by the auditor
Statements by independent parties	→ Confirmation by a letter
Statements by entity personnel	→ Verbal inquiry and written representations
Documents prepared by independent parties	→ Examination of documents (vouching or tracing)
Documents prepared by the audited entity	→ Examination of documents (vouching or tracing)
Data relationships	→ Scanning Analytical procedures

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[80] ISSAI 4000.169

[81] William F. Messier, Jr., Auditing and Assurance Services: A Systematic Approach, third edition, p. 152

[82] Jack C. Robertson and Timothy J. Louwers, Auditing and Assurance Services, tenth edition, p. 93

Examination of documents: Vouching

Vouching is taking information from one document or record backwards to an asset, document, or record that was prepared earlier. For example, auditors might vouch for information in a computer-generated report to the source documents from which the information was input to the entity's information system and verify the validity of the information.

Examination of documents: Tracing

Tracing is taking information from one document, record, or asset forward to a document or record that was prepared later. For example, if the auditor counts inventory, they would trace their count forward to the entity's inventory records and verify the completeness of the inventory as required by the records.

Scanning

Scanning is the way auditors exercise their general watchfulness for unusual items or events in the audited entity documentation. In general, scanning is the 'keeping eyes open' approach of looking for anything uncommon. Auditors need to consider that the scanning procedure generally does not produce direct evidence itself, but it can assist them in raising questions for which they need to obtain evidence.

6.4 DETERMINING THE SAMPLE SIZE

ISSAI 4000.172 states, '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.'

Audit sampling is defined as the application of audit procedures to less than 100% of items within a population relevant to the audit. A sample may be quantitative or qualitative, depending on the audit scope and the need for information to analyse the subject matter from several angles.

Quantitative sampling is used when the auditor seeks to draw conclusions about the whole population by testing a sample of items selected from it. In quantitative sampling, the sample risk must be reduced to an acceptable low level. However, the technical approach to quantitative sampling may require the use of statistical techniques. If the audit team lacks the skills to apply them, an expert statistician may be necessary.

Qualitative sampling is a selective procedure conducted as a deliberate and systematic process to identify the factors of variation in the subject matter. The auditor might sample based on characteristics of individuals, groups, activities, processes or the audited entity as a whole. Qualitative sampling always requires careful assessment and a thorough understanding of the subject matter.

When the auditor selects cases for in-depth study, it usually results in relatively small samples that can answer more exploratory questions and provide new information, analyses and insights into the subject matter. It may be appropriate to use risk-based sampling instead of a statistical approach when selecting items for testing; for instance, when addressing a specific significant risk.

Selecting samples for testing

When deciding which sample items to test, the auditor can:

- Select all items (100% examination);
- Select specific items; or
- Use audit sampling.

The choice of a particular method is a matter of an auditor's professional judgment based on risk assessment, materiality, audit efficiency and cost. But the chosen method should be effective in achieving the purpose of the audit procedure.

When to select all items

Selecting all items is appropriate when the number of items is small but high in value, when the risk is high or when computer-assisted audit techniques (CAATs) allow all items to be tested efficiently. It is more common to conduct substantive testing (tests of details) than tests of controls.

When to select specific items

The auditor selects certain items from a population based on their specific characteristics. These are typically high-value or high-risk items (e.g., relatively high or low amounts) or items that represent a large proportion of the subject matter. It is useful for tests of controls and substantive testing, and also to gain an understanding of the entity or to confirm the auditor's risk assessment. While it is an efficient method of gathering audit evidence, it is not comparable to audit sampling, and so the results cannot be projected to the entire population. However, it may play a role as part of an audit approach that provides reasonable assurance without using audit sampling methods.

When to use audit sampling

The sampling method used to select the sample should match the characteristics of the population. The audit team should decide the most appropriate method of selecting the samples. The auditor can determine the suitable sampling method by using the decision tree in Figure 6.1 below.

FIGURE 6.1:
Decision tree – determining the appropriate sample selection method
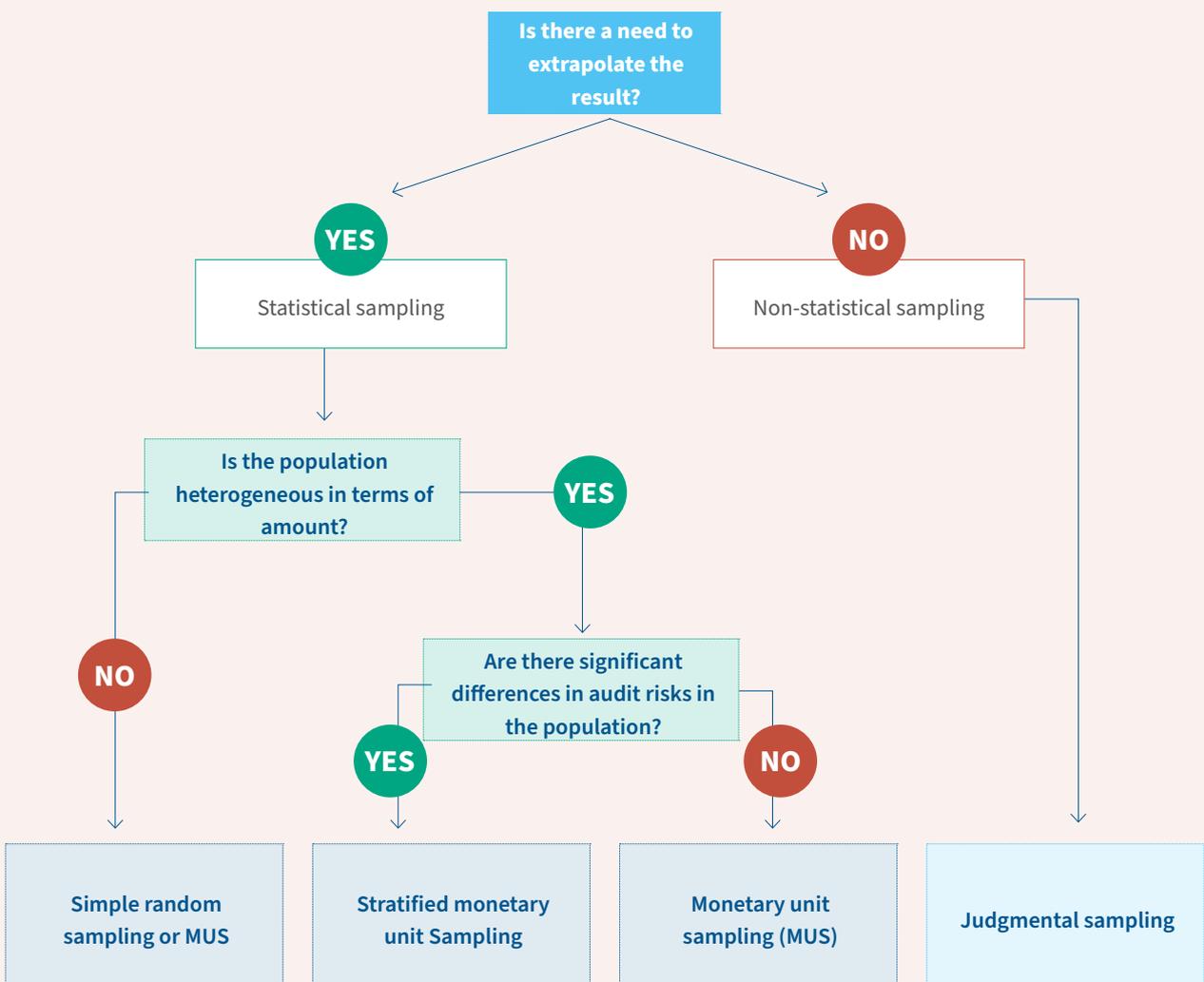
Judgmental sampling (risk-based sampling): This involves selecting items from a population in accordance with predetermined and documented criteria based on the auditor's judgment. Judgmental or risk-based sampling cannot be used if the objective of the sample is to extrapolate the results. When reporting results, auditors should ensure readers are not misled into thinking the results are representative of the population.

Simple random sampling: The main characteristic of simple random sampling is that all transactions or sampling units have the same chance of being selected for testing. A high-value transaction is no more likely to be chosen than a low-value one. While the method is the most straightforward to apply, its use for tests of detail is generally restricted to situations in which the sampling units comprising an area of the subject matter are relatively homogeneous.

Systematic sampling is a method of statistical sampling in which every item has an equal chance of selection. The practical implementation of a systematic sampling method uses a random starting point and an average sampling interval to progress through the expenditure. For example, if the auditor wishes to select 100 items from a population of 20,000 items, the uniform interval is every 200th item. The auditor selects the first item in the first interval and then every 200th item thereafter. The first item is chosen randomly.

Monetary unit sampling (MUS): A statistical sampling method in which a high-value transaction is more likely to appear in the sample than a low-value one. The chance of a transaction being selected is directly proportional to its size. Any transaction above the average sampling interval will certainly be selected. Monetary unit sampling is more widely used than simple random sampling because it is usually more efficient, as the margins of uncertainty in the estimates of error are generally narrower.

However, the calculations involved in extracting a monetary unit sample can be cumbersome, and the method is practical if it can be automated. Also, statistically, this method is valid only for populations with low error rates.

Stratified MUS: Stratified monetary unit sampling divides the population into several subgroups (strata). The strata have to be predefined according to different characteristics within the population, e.g., risk. The auditor should use professional judgment when determining these characteristics, including his/her knowledge of the population subject to audit. In each stratum, a number of items are selected with MUS. The number of items to be selected can be different in every stratum.

For the particular type of engagement and subject matter, using any of these methods, the auditor selects the samples to perform audit procedures on the identified risks to gather sufficient and appropriate audit evidence.

Considerations in selecting samples for testing

It is important to note that determining sample size requires documenting the underlying considerations of the subject matter. The support for the sample size used in an audit is based on auditor judgment. It depends on factors such as the significance of the control being tested or the risk of material non-compliance, both of which are important in documenting the application of sampling procedures.

Also, SAIs may use their internal guidance, which results in a sample size that is different from the approach suggested here. When an auditor determines a sample size using SAI-suggested methods, the basis for that determination is also important for documenting the sampling applications and procedures.

6.5 EVALUATING AUDIT EVIDENCE AND FORMING CONCLUSIONS

ISSAI 4000.179 states, 'The auditor shall compare the obtained audit evidence with the stated audit criteria to form audit findings for the audit conclusion(s).' For a balanced and objective view, the evaluation process entails considering all evidence provided in relation to the audit findings. By evaluating the scope of work performed, the auditor determines whether s/he can draw a conclusion. If the scope of work is insufficient, the auditor might consider performing further procedures or modifying the opinion or conclusion due to a scope limitation.

Whether the evidence gathered is sufficient and appropriate

The evidence-gathering process continues until the auditor is confident that sufficient and appropriate evidence exists to support the agreed level of assurance that will support the auditor's conclusion or opinion.[83] The auditor maintains professional scepticism throughout the audit to reduce the risks of:

- Overlooking unusual circumstances;
- Overgeneralising when drawing conclusions from observations; and
- Using inappropriate assumptions in determining the nature, timing and extent of procedures and evaluating the results thereof.

In assessing the evidence gathered, the auditor exercises professional scepticism by questioning inconsistent evidence and the reliability of documents and responses to inquiries. Also, the auditor considers the sufficiency and appropriateness of evidence obtained in light of the circumstances.

The auditor should not disregard experience with the honesty and integrity of those who provide evidence. Nevertheless, a belief that those who provide evidence are honest and have integrity does not relieve the auditor of the need to maintain professional scepticism during the audit. It is also equally important to consider:

- The nature, timing and extent of procedures used to obtain evidence
- Whether sufficient appropriate evidence has been obtained
- Whether more needs to be done to achieve the objectives of relevant auditing standards
- The appropriate conclusions to draw based on the evidence obtained

In the direct reporting engagement, auditors plan audit procedures to gather evidence on the risks identified at the planning phase. The audit strategy and audit plan document include the audit planning matrix (Exhibit 5.7), which lists all risks for audit testing and the audit procedures applied to them. Once the auditor performs the audit procedures for the identified risks, based on the information and analysis of those, the auditor formulates audit findings.

Audit findings and observations

An audit finding describes the compliance deviation, based on the information gathered during fieldwork, between the existing situation and the criteria. The common elements of a finding are criteria (authorities to comply with), condition (what is the situation found vis-à-vis the criteria), cause (why there is a deviation from the criteria) and effect (what are the consequences of the non-compliance).

The findings, information obtained during the audit, conclusions, and recommendations can be recorded in the findings matrix. The findings matrix is a useful tool to facilitate the assessment of the findings, whether they are based on sufficient, appropriate evidence, as well as to prepare a coherent audit report.

The narrative of the findings is based on the substantive tests of details (or the procedures performed) for all identified risks. The table in Illustration 6.2 below shows the elements of an audit findings matrix.

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[83] ISSAI 4000.150

ILLUSTRATION 6.2
Findings matrix template

Risk/Audit question:			
Finding			
Audit criteria	**Condition/evidence**	**Cause**	**Effect**
Conclusion:			
Recommendation (if applicable):			

The auditor determines the causes of the non-compliance and its effect. The effect of non-compliance may be monetary or other losses to the entity, and it can also point to the party responsible for the non-compliance. While identifying the cause is important, it is more important to determine the root cause of a particular non-compliance.

The auditor can make appropriate and implementable recommendations based on the identified root cause . If the root cause cannot be determined, a recommendation will not address the core problem, and the entity will fail to rectify the particular non-compliance. Identifying the root cause requires the auditor to focus on the underlying cause of the non-compliance, rather than the surface-level or obvious cause. The root cause analysis process is explained below.

Root cause analysis
The root cause is identified with the use of appropriate root cause analysis tools, e.g., brainstorming, fishbone diagram, flowcharting or answering the 'five whys.' The five whys tool is the simplest root cause analysis tool. It uses a question-asking method to explore the cause-and-effect relationship underlying the problem. Essentially, the auditor keeps asking 'why' until a meaningful conclusion is reached. Generally, a minimum of five questions should be asked, although additional questions may be required if the actual cause has not yet been identified. An illustrative example[84] is provided below.

A finding of non-compliance	The entity's fleet of vehicles did not meet the set availability target: it failed to meet the criteria to provide the required service with the delivery of vehicles.	
Obvious cause	The entity did not have enough vehicles.	
Recommendation	Aimed at a symptom or apparent cause:	
	The entity should ensure that the fleet of vehicles meets the availability target.	
Identifying the root cause	Identifying the root cause of the non-compliance for vehicle service using the 'five whys' tool:	
	Why 1	The vehicles were often unavailable due to mechanical problems.
	Why 2	There were not enough technicians on site to fix the mechanical repairs.
	Why 3	Too few technicians have completed training in recent years.
	Why 4	Not enough instructors were available to provide the required training.
	Why 5	Many instructors retired in the same year, without a succession plan or recruitment strategy.
Recommendation	Aimed at the root cause:	
	The entity should establish a succession plan and recruitment strategy to support vehicle maintenance activities.	

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[84] https://www.caaf-fcar.ca/images/pdfs/research-publications/RootCauseAnalysisEN.pdf

By answering the five 'whys' using root cause analysis, the auditor found that the entity was unable to provide vehicle service due to a budget cut to driver training. Besides, there were not enough skilled drivers for service delivery. Had the auditor ended the analysis with the surface-level or obvious cause, the recommendation would have been for the entity to ensure that vehicle service is provided as per the required rules. Since this does not address the core problem of the non-compliance, it would not lead to any improvement in the entity's system, and the non-compliance would recur.

Considering materiality

While completing the findings matrices for the identified risks, the auditor determines if the non-compliances are material or not. Here, the auditor applies the concept of materiality for value and nature or context. ISSAI 4000.37 states that the auditor uses materiality in determining the extent of audit procedures to be performed and in the evaluation of audit evidence. In evaluating evidence and concluding the audit, the auditor uses materiality to assess the scope of work and the level of non-compliance, and thereby determine the impact on the conclusion or opinion.

If the non-compliance can be quantified, the quantitative materiality determined at the planning stage can be applied. Where the non-compliance is non-monetary and qualitative, the auditor could apply the materiality threshold identified at the planning stage. The auditor uses professional judgment to determine if non-compliance is material or not by considering:

The amount involved…	can be a monetary amount or other measures such as the number of people involved, delays in days or time, etc.
The visibility and sensitivity…	of the subject matter under audit, and the effects and consequences of non-compliance
Expectations…	of the legislative body, the general public or other stakeholders and end users of the audit report
Nature and significance…	of the authorities governing the subject matter

The auditor can document the findings on the identified risks using the working paper template provided in **Exhibit 6.3**: Audit findings matrix. Below is an illustrative example of a findings matrix prepared based on the example of operations of a city council provided in planning (section 5.2).

Example: Performing audit procedures for operations of the city council

Risk/audit question: The entity may not have provided adequate fire security arrangements in the completed buildings.			
Finding			
Audit criteria	**Condition/evidence**	**Cause**	**Effect**
As per clause 1.1.20xx of the 20xx-Fire Safety, 'All new buildings should be provided with at least one fire extinguisher on each floor.'	The audit team checked and verified the approved building drawings. Also, the team compared the implementations of the requirement during a physical verification to selected sites from 20/7/20xx to 22/7/20xx in conformity with clause 1.1.20xx. The team found that in the majority of the buildings, fire safety equipment was not in place as required by the clause.	The city authority didn't enforce the requirement prior to approving the application of the building drawings and designs. Also, the clause didn't include any provision for a penalty for not having a fire extinguisher; the city authority couldn't impose a penalty for such cases.	Due to this, the completed buildings are vulnerable to fire and pose a risk to human life.
Conclusion The entity didn't comply with the requirements to have at least one fire extinguisher on each floor of the building as per 1.1.20xx of the 20xx-Fire Safety.			
Recommendation The management should put in place proper controls to ensure that the provisions of the clause are strictly complied with in future approvals, and enforce penalty rules against non-compliance in line with the amended 1.1.20xx of the 20xx-Fire Safety.			

Forming an overall conclusion on the subject matter

ISSAI 4000.184 states, '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 forms the overall conclusion, or audit opinion, in evaluating all relevant evidence in relation to the identified materiality. Based on materiality, the auditor considers whether the audit findings are material enough to conclude on the subject matter.

In evaluating audit results of subject matters with non-monetary compliance attributes, the qualitative materiality threshold (the tolerable level of non-compliance) set at the planning stage is to be used. A threshold can also be set for each area of the subject matter as well as for the subject matter as a whole. A materiality threshold for each area of the subject matter, in addition to the overall materiality threshold, may be helpful for evaluating the sample results and forming a conclusion.

Example
If the subject matter is the procurement practice of the Ministry of Infrastructure: → Overall threshold (tolerable level of non-compliance) could be set at 4%. → The threshold for individual areas of the subject matter may be set as: → Procurement planning 3%, sourcing 5%, contract management 4%.

The threshold for each area has to be set after considering the risks in each area, the status of controls, and the entity's past compliance record in these areas.

Forming a conclusion based on the test of controls is a process common to both attestation engagements and direct reporting engagements. It is the usual audit process followed to arrive at an audit conclusion when the test of controls and statistical sampling are used for subject matters that are value-driven, and instances of non-compliance can be quantified. Suppose statistical sampling is applied in a direct reporting engagement. In that case, if the subject matter is value-driven and the non-compliances are quantifiable, the same process can be followed to form the conclusion.

In formulating the overall conclusion, the auditor has to calculate the actual non-compliance rate. For that, the auditor determines the instances of non-compliance observed in the tests. For example, if the total sample size tested was 40, and the instances of non-compliance identified were 5, then the actual non-compliance rate would be (5/40) x 100 = 12.50%. If judgmental sampling was used, the auditor might directly compare this non-compliance rate with the tolerable level of non-compliance (threshold) set for the subject matter. If the non-compliance rate exceeds the threshold, the auditor may conclude that the subject matter is not in compliance with the established criteria.

However, it may be that the identified instances of non-compliance are from one particular area of the subject matter and not spread across the entire subject matter. In other words, the non-compliance is not pervasive. In that case, the auditor has to modify the conclusion in such a way that it is clearly communicated.

When the auditor can quantify the non-compliance, the value of the non-compliance is compared against the qualitative materiality level set to form the conclusion. The auditors also consider the pervasiveness of the non-compliance and may modify the conclusion depending on the circumstances.

6.6 ENSURING QUALITY AT THE AUDIT FIELD-WORK STAGE

Ensuring quality during fieldwork and in the gathering and evaluation of audit evidence is a fundamental component of the audit practice. Upon completion of the fieldwork, the audit supervisor should review all aspects of the audit tasks performed during the audit – including the audit tests carried out, the findings, and the working papers – and should document such reviews. It is helpful, during this review process, to identify the changes and improvements needed for current and future audits. The reviewer may consider the checklist provided in **Appendix 6-A** to quality review the audit fieldwork.

CHAPTER 7

REPORTING AND FOLLOW-UP COMPLIANCE AUDITS

This chapter covers the reporting and follow-up phases of the compliance audit process. It describes the principles of reporting, the structure, and the form and content of reports for both direct reporting and attestation engagements.

The SAI provides information to the intended users (Figure 7.1) through its audit reports on whether the audited entities have complied with legislative decisions, laws, legal acts, policies, established codes, and agreed-upon terms. The auditor performs audit procedures to reduce audit risk and ensure that the conclusion or opinion provided in the report is appropriate in the circumstances of the audit. This assurance, in effect, forms the basis for the compliance audit report.

FIGURE 7.1:
Users of SAI audit reports

The auditors begin reporting by drafting preliminary findings or observations. The SAI management approves the initial observations, after which the team completes the contradiction procedures with the audited entity. The auditor finalises the report for SAI approval, issues it, and submits it to the respective users according to the SAI's mandate.

7.1 PRINCIPLES OF REPORTING

To ensure the report is produced in accordance with quality standards and is relevant to all its users, it should conform to the five principles of reporting. ISSAI 4000.202 states, 'The auditor shall prepare an audit report based on the principles of completeness, objectivity, timeliness, accuracy and contradiction.'

ILLUSTRATION 7.1:
Principles of reporting

OBJECTIVITY

→ requires the auditor to apply professional judgment and scepticism to ensure that the report is factually correct and that findings and conclusions are presented in a relevant, fair and balanced manner.

COMPLETENESS

→ requires the auditor to consider all relevant audit findings before issuing the report. The relationship between audit objectives, findings and conclusions needs to be completely and clearly stated.

TIMELINESS

→ requires the auditor to prepare the report in due time when the findings are applicable and relevant for the intended users.

ACCURACY AND CONSULTATION

→ require the auditor to check the accuracy of facts with the audited entity, and to ensure that the findings portray a correct and logical picture.

CONTRADICTION

→ requires that the auditor incorporate responses from the responsible party as appropriate and give answers to and assessments of the responses.

The key to an excellent report is effective communication, with clear and objective findings and conclusions on the audit objectives. It allows the reader to understand what was done, why and how. It also provides practical recommendations, without impairing the auditor's objectivity.

Proper planning and conducting with adequate quality control measures throughout the process provides the basis for a quality compliance audit report. Additionally, reports should be clear – using simple language for easy understanding, free of vagueness or ambiguity, and be concise and balanced. In the report, the auditor should present persuasive arguments with illustrative examples. Such a report helps the responsible party take appropriate corrective actions to address instances of non-compliance and helps the auditor to plan following up on its findings. In deciding on how to prepare the report, the auditor considers the following:

Users' needs	SAI mandate	Relevant legislation and regulation
Level of assurance provided	Type of engagement	SAI's reporting practice
	Complexity of the reported issues	

7.2 ELEMENTS OF A COMPLIANCE AUDIT REPORT

Considering the types of engagement and the degree of assurance provided, compliance audit reports can primarily be for reasonable assurance – either a direct reporting engagement or an attestation engagement. The structure and content of these two types are described below. To determine the length and structure of its compliance audit reports, the audit team should consider the SAI mandate and legal framework, along with the ISSAI requirements.

The elements of the audit report for a direct reporting engagement[85] and attestation engagement[86] are:

Direct reporting engagement	Attestation engagement
1. Title	**1.** Addressee
2. Identification of the auditing standards	**2.** Addressee
3. Executive summary (as appropriate)	**3.** Identification of the auditing standards and level of assurance
4. Description of the subject matter and the scope (extent and limits of the audit)	**4.** Description of the subject matter information, and when appropriate, the underlying subject matter
	5. Extent and limits of the audit, including the period covered
	6. Responsibilities of the responsible party and the auditor
5. Audit criteria	**7.** Audit criteria
6. Explanation and reasoning for the methods used	**8.** A summary of the work performed and methods used
7. Findings	**9.** Opinion or conclusion
8. Conclusion(s) based on answers to specific audit questions or opinion	**10.** Replies from the audited entity (as appropriate)
9. Replies from the audited entity (as appropriate)	**11.** Report date
10. Recommendations (as appropriate)	**12.** Signature

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85 ISSAI 4000.210

86 ISSAI 4000.218

Some of these elements are common for both direct reporting and attestation engagement. Some elements are specific to each type of engagement. These are explained below.

Elements common to both direct reporting and attestation engagements

Title	The title of the report briefly mentions the audit subject matter in a way that can be clearly understood by readers.
Identification of the auditing standards applied and the level of assurance	In its audit reports, the SAI declares which standards it follows when conducting the audit. Also, in the audit report, the SAI should refer to the auditing standards it followed in conducting the particular audit.
	A direct reporting engagement report differs from an attestation engagement report in the requirement regarding conveying assurance.
	In a direct reporting engagement, the auditor might not give an explicit statement of assurance on the subject matter but must provide the users with the necessary degree of confidence. The auditor explicitly explains how the findings, criteria and conclusions were developed in a balanced and reasoned manner, and why the combinations of findings and criteria result in a particular overall conclusion or recommendation.
	In an attestation engagement report, opinions and conclusions should explicitly convey the level of assurance.
Description of the subject matter and the scope	The subject matter is described in the audit report. The report's introduction sets out the audit scope in the form of a clear statement of the audit's focus, extent and limits. It also includes the period covered by the audit.
Audit criteria	The criteria against which the subject matter is assessed should be identified in the auditor's report. The criteria may be included in the report itself or the report may refer 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 applied in the audit are not readily identifiable or have had to be derived from relevant sources, the criteria are clearly stated in the relevant section of the auditor's report. In cases where the criteria are conflicting, the conflict is explained.
Explanation and reasoning for the methods used	The report should include a clear statement on the procedures performed to gather evidence in answering the audit questions. This will enable a user to read and follow the report and have confidence that the conclusions made are correct.
	It is important to write the methodological summary in an objective way that allows intended users to understand the work done as the basis for the auditor's conclusion. However, the summary should not be so brief as to make it difficult to understand the auditors' work, especially how the auditors arrived at a conclusion or opinion.

Conclusion(s) or opinion based on answers to specific audit questions	The conclusion or opinion is expressed as an answer to specific audit questions. The nature of the wording may be influenced by the SAI mandate and the legal framework under which the audit is conducted. ISSAI 4000.191 states, 'The auditor shall communicate the conclusion in an audit report. The conclusion can be expressed either as an opinion, a conclusion, an answer to specific audit questions or recommendations.' In a direct reporting engagement, the auditor provides assurance by measuring the subject matter against the criteria and forming a conclusion. 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. The conclusion is expressed in the form of findings, answers to specific audit questions, recommendations or opinions. For attestation engagements, the level of assurance will be conveyed by the appropriate use of standardised audit opinions. Forms of opinion and conclusion for attestation engagement are explained in section 7.2.
Replies from the audited entity (as appropriate)	Incorporating the responses to the findings from the audited entity is part of the principle of contradiction. It involves agreeing on the facts with the audited entity to help ensure that findings are complete, accurate and fairly presented. It also involves, as appropriate, incorporating the audited entity's response to the matters raised, whether verbatim or in summary. Timely clearance of the findings provides a sound basis for the final report and reduces the time required to reach agreement with the audited entity. The team sends the draft report, with the SAI approval, to the audited entity for comment. During the conducting phase of the audit, the team has already discussed the individual findings with the entity. With this, the entity was up to date on the audit's progress. The medium used to present the findings to the audited entity can be based on the SAI's regular forms, e.g. a management letter or draft findings. The auditee is required to respond to the draft report. Once the team receives comments from the entity, the auditor analyses the response and ensures that valid issues raised by the auditee are taken into account while finalising the report. Based on the SAI's legal framework, the auditor may publish the report with the comments in whole, or in a summary or an edited version, or not include the comments.

Elements specific to a direct reporting engagement

Executive summary	The executive summary of the work performed and methods used helps the intended users understand the auditor's conclusion. Hence, the executive summary needs to give the reader a brief explanation of how the audit was performed. The executive summary includes a paragraph on the entity's background, explaining the main topic and its importance. It also consists of the objective, audit questions and audit approach, and describes the key audit findings and conclusions in a summary form, easy to read and understand. From this, the reader gets an overview of the topic's critical issues. The executive summary includes the audit's main recommendations and a statement that confirms that the audited entity had the opportunity to comment on the report. The executive summary typically ranges from two to three pages but can be shorter, depending on the particular audit.
Findings	The findings section includes the auditor's description of the gathered evidence compared with the criteria. The audit finding is structured to assist the reader to understand the audit question, with analysis of risk, based on the evidence, to the conclusion on the problem. The auditor uses the completed audit finding matrices as working papers (explained in Chapter 6) to draft the findings. If there is significant supporting information for the audit findings, the auditor may include that information in the appendices.
Recommendations	The report includes, as appropriate, recommendations designed to result in improvements. While such recommendations may be constructive for the audited entity, they should not be so detailed that the auditor's objectivity may be impaired in future audits. Suppose the auditor makes a specific recommendation and the responsible party does not implement that, but considers another option. In that case, the auditor may, in subsequent audits, be tempted to judge this as non-compliance. In such instances, the key is to determine whether recommendations leave room for the entity to use whatever mechanism it considers suitable in the circumstances to achieve compliance. It is a good practice to discuss the recommendations with the entity. The auditor might assume that the suggested recommendation is useful for the entity, but during the discussion, the entity can clarify the practicality of implementing the recommendation or explain the difficulties of doing so. Based on the discussion, the auditor can modify and finalise the recommendations.

Elements specific to an attestation engagement

Addressee	An addressee identifies the party or parties to whom the audit report is directed. The audit report is ordinarily addressed to the responsible party, but in some cases, there may be other intended users. The intended users may be legislative or oversight bodies, those charged with governance, the public prosecutor or the general public.
Extent and limits of the audit, including the period covered	The report sets out the audit scope as a clear statement of the audit's focus, extent and limits in terms of the subject matter's compliance with the criteria. The introduction also includes the period covered by the audit.
Responsibilities of the responsible party and the auditor	Identifying relative responsibilities informs the intended users that the responsible party is responsible for the underlying subject matter. It also confirms that the measurer or evaluator is responsible for the measurement owr evaluation of the underlying subject matter against the applicable criteria and that the auditor's role is to independently express an opinion or conclusion about the subject matter information. These responsibilities can be expressed as follows: **Responsibility of the responsible party:** According to [the terms of the agreement with the organisation XYZ dated xx.xx.20XX], management of government agency ABC is responsible for [preparing complete accounts in compliance with the terms of the agreement]. **Responsibility of the auditor:** Our responsibility is to independently express a conclusion or opinion on [the project accounts] based on our audit. Our work was conducted in accordance with the [Compliance Audit ISSAIs]. Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether [the use of the project funds is 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 and appropriate evidence to support our conclusion. The procedures performed depend on the auditor's professional judgment, including assessing the risk of material non-compliance, whether due to fraud or error. The audit procedures we performed are those we believe are appropriate in the circumstances. We believe that the audit evidence gathered is sufficient and appropriate to provide the basis for our conclusion.
Report date	The audit report should be dated. The auditor should ensure that the report is not dated before s/he has obtained sufficient and appropriate audit evidence to support the opinion or conclusion.
Signature	The audit report should be signed by someone with appropriate authority to do so, namely the Head of the SAI, or someone to whom authority has been delegated.

Opinion or conclusion in an attestation engagement

In an attestation engagement, the auditor provides assurance by making a clear statement of the level of assurance through either standardised opinions or conclusions.

In formulating the opinion, the auditor considers the level of assurance provided. An opinion is a clear written statement expressed in a standardised format, either unmodified or modified. It is stated in the audit report whether instances of non-compliance are pervasive.

Unmodified opinion

Where no material instances of non-compliance have been identified, the opinion is unmodified.[87] An example of the form for an unmodified opinion for a reasonable assurance engagement (where appropriate wording is inserted in the brackets as applicable) may be as follows:

Unmodified opinion
'In our opinion, [the audited entity's subject matter] is in compliance, in all material respects, with [the applied criteria].'

Modified opinion

The auditor modifies his/her opinion[88] in cases of:

a. Material instances of non-compliance, and for

b. Scope limitation.

a. For the material instances of non-compliance, depending on the extent of the non-compliance, this may result in:

i. A qualified opinion	ii. An adverse opinion
If compliance deviations are material, but not pervasive, the opinion is: 'Based on the audit work performed, we found that except for [describe exception], the audited entity's subject matter is in compliance, in all material respects with [the applied criteria]…', or	If compliance deviations are material and pervasive, the opinion is: 'In our opinion, [the subject matter] is not in compliance, in all material respects with (the applied criteria) … and compliance deviations are pervasive.'

b. For scope limitation, depending on the extent of the limitation, this may result in:

iii. A qualified opinion	iv. A disclaimer
If the auditor is unable to obtain sufficient and appropriate audit evidence, and the possible effects are material, but not pervasive, the opinion is: 'In our opinion, except for [describe exception], the auditor was unable to obtain sufficient and appropriate audit evidence, and the possible effects are material, but not pervasive.', or	If the auditor is unable to obtain sufficient and appropriate audit evidence on compliance with authorities and the possible effects are material and pervasive, the opinion is: 'We do not express an opinion on the subject matter. We have not been able to obtain sufficient and appropriate audit evidence to provide a basis for an opinion…'.

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[87] ISSAI 4000.193

[88] ISSAI 4000.194

Conclusion

Conclusions in the attestation engagement are presented in the same manner as in a direct reporting engagement. Conclusions expressed in a form appropriate to a reasonable assurance engagement include the following:

- When expressed in terms of the underlying subject matter and the applicable criteria, 'In our opinion, the entity has complied, in all material respects, with criteria'
- When expressed in terms of the subject matter information and the applicable criteria, 'In our opinion, the forecast of the entity's activity is properly prepared, in all material respects, based on criteria'

Limited assurance engagement

In a limited assurance engagement, the format of an unmodified opinion may be:

'Based on the work performed described in this report, nothing has come to our attention that causes us to believe that the subject matter is not in compliance, in all material respects, with the [applied criteria].'

A modified opinion could state that:

'Based on the work performed described in this report, except for [describe exception], nothing has come to our attention that causes us to believe that the subject matter is not in compliance, in all material respects, with the [applied criteria].'[89]

In a limited assurance engagement, the auditor gathers sufficient and appropriate evidence to address the engagement objective; however, the procedures are limited compared with what is necessary for a reasonable assurance engagement.

7.3 REPORTING BY SAIS WITH JURISDICTIONAL POWERS

ISSAI 4000.221 states, '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:'

Report structure: SAIs with jurisdictional powers
1. Identification of the responsible parties and the audited entity
2. The responsible person(s) involved and their responsibilities
3. Identification of the auditing standards applied in performing the work
4. Responsibilities of the auditor
5. A summary of the work performed
6. Operations and procedures, etc., that are affected by non-compliance acts and possible unlawful acts. This needs to include, as appropriate: → A description of the finding and its cause → The legal act which has been infringed (the audit criteria) → The consequences of the non-compliance acts and possible unlawful acts
7. The responsible persons and their explanations regarding their non-compliance acts and possible unlawful acts, when appropriate
8. The auditor's professional judgment that determines whether there is personal liability for non-compliance with acts
9. The value of the loss, misuse or waste created and the amount to be paid due to personal liability
10. Any measures taken by responsible persons during the audit to repair the loss, misuse or waste created
11. Management's arguments on the non-compliance or unlawful acts

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In audits conducted by SAIs with jurisdictional powers, the users of compliance audit reports include the prosecutor or those responsible for dealing with judgment issues within the SAI.

SAIs with jurisdictional powers may determine personal liability for acts of non-compliance. Usually, these are the proposals and final decisions – on individual liability and sanctions – taken in a jurisdictional process. Personal liability can be measured by the extent of the participation of the person in a non-compliant (illegal, unnecessary, excessive, extravagant, unconscionable) transaction as indicated in the transaction's documents that s/he signed.

In the report, the auditor needs to explain the methods used to determine whether each responsible person involved in administering, managing, using, or controlling public funds or assets is liable for non-compliance.

7.4 REPORTING SUSPECTED FRAUD AND UNLAWFUL ACTS

ISSAI 4000.225 states, '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.'

Reporting suspected unlawful acts

While detecting potential unlawful acts, including fraud, is not the primary objective of conducting a compliance audit, auditors do include fraud risk factors in their risk assessments. Auditors remain alert to indications of unlawful acts, including fraud, in carrying out their work.

Auditors may consider consulting with legal counsel or appropriate regulatory authorities. Furthermore, they may communicate their suspicions to the appropriate levels of management or those charged with governance, and then follow up to ascertain that appropriate action has been taken. 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 regarding instances of non-compliance related to fraud or serious irregularities.

A court of law can determine whether a particular transaction is illegal and constitutes a criminal offence. But SAIs with jurisdictional powers may also conclude that a specific transaction is prohibited. The SAI may justify imposing sanctions on the responsible person and determining the reimbursement of funds, misappropriated assets and undue or improper payments.

Although auditors do not determine whether an illegal act constitutes a criminal offence or civil liability has occurred, they do have a responsibility to assess whether the transactions concerned comply with applicable laws and regulations and whether they constitute infringements that will lead the court to impose sanctions or reimbursement of undue or improper payments or misappropriated assets.

Fraudulent acts, by their nature, are not in compliance with relevant regulations. The auditor may also determine that transactions where fraud is suspected but not yet proven are not in compliance with the authorities. Fraud results typically in the qualification of the compliance opinion in the auditor's report.

SAIs with jurisdictional powers

If suspicion of unlawful acts arises during the audit, the auditor may communicate this to the appropriate levels of management and those charged with governance. Those charged with governance are likely to be administrative bodies higher up in the reporting hierarchy. Where applicable and reasonable, the auditor may 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. The auditor may also report such incidents directly to the relevant law enforcement authorities.

7.5 ENSURING THE QUALITY OF THE AUDIT REPORT

Ensuring the quality of the audit report by adhering to reporting principles is essential for the auditor. All findings and conclusions must be supported by adequate, reliable audit evidence in the audit working papers. Reported audit issues need to be adequately analysed and concluded on. Viewpoints of auditees on significant matters raised during the audit should be mentioned and discussed in the report. The auditor should acknowledge material conflicting evidence along with an explanation of why it was rejected or otherwise not reflected in the report's conclusions. The standards of materiality and significance will depend on the nature of the audit and the type of report or other output.

The draft report prepared by the team should be carefully reviewed for adequacy by the team leader or supervisor and by an experienced auditor who is independent of the audit team. The team should respond appropriately to any comments by this reviewer. This review, any comments by the reviewer and actions taken in response should be documented and retained in the audit working papers.

After the draft report is reviewed internally, it should be provided to the auditee for review and comment within a specified timeframe. Comments received from an auditee should be carefully considered by the auditor. Factual disagreements should be resolved, which may require additional audit work. The audit report should be adjusted, if appropriate, in response to the auditee's comments.

The reviewer can use the checklist provided in **Appendix 7-A** to quality review the audit report.

7.6 COMMUNICATING THE REPORT TO THE STAKEHOLDERS

It is a good practice for the SAI to develop a communication strategy or policy to provide guidance on how to engage with the audited entity and relevant stakeholders during the reporting process. Communication with key stakeholders is explained below.

The audited entity	The communication process between the auditor and the audited entity begins at the planning stage of the audit and continues throughout the audit process. The SAI must always provide the audited entities with an opportunity to comment on the audit findings, conclusions and recommendations. After issuing the draft report, the SAI should ask the entity management to provide, within a specified time frame, comments on agreement or disagreement with the validity and completeness of the draft report's content.
	The audit team may meet with entity officials to discuss the entity's comments, to gain a full understanding of the comments and to obtain any additional significant information related to the comments. If conflicts occur, efforts must be made to resolve contradictory opinions to make the final picture as true and fair as possible. Such meetings are usually limited in number and should be scheduled within a period that meets the SAI's report production schedule.
Legislative body	Communication with the legislative body, e.g. the Parliament, is equally important because it is the Parliament that will use the SAI's reports to improve government management and accountability. If reports are ignored or messages are misunderstood, audit resources could be wasted and the SAI's credibility could be called into question.
	SAIs assist the legislative bodies, such as the Public Accounts Committee (PAC), by debriefing the Parliament members and providing relevant information regarding reported audit findings. In addition to prior communication, it is vital that SAI representative(s) attend the PAC hearings where audit reports are discussed.

The media	When the report is tabled in Parliament, it becomes a public document. The report and news releases are posted in the media. The SAI should ensure that the information provided to the media is timely, accurate and clear. In providing the information, the SAI should be responsive, helpful and informative, without compromising its independence or political neutrality or offending parliamentary privilege. Communication with the media is facilitated by: → Responding to media inquiries; → Developing news releases in conjunction with audit teams; → Organising and managing media events such as news conferences and interviews; → Assisting staff in developing questions and answers in media lines; → Providing staff with media training; → Monitoring news and public discussions about the SAI; → Informing senior management about emerging issues in the media; and → Conducting media analyses to assist in improving message development.
Citizens and other stakeholders	Citizens are a source of ideas for public sector auditing, a source of demand for auditing and users of the audit reports. They may be contacted directly or through non-government organisations that represent them. Depending on the circumstances in the SAI's country, this communication could include a mix of television interviews, articles, leaflets and the SAI's website. Other relevant stakeholders are representatives of the academic community. They have expert knowledge in specific audit areas and may provide a more objective view, less restricted by personal interest. Non-government organisations can be a useful source of ideas. They may have conducted their research through surveys and case studies, and may have a range of relevant contacts. Civil society can be motivated to put pressure on the legislature to act, particularly if the SAI is providing information on a topic that is of their interest.

7.7 AUDIT FOLLOW-UP

At some time after an audit report is issued, an SAI should take appropriate steps to determine what action, if any, an auditee has taken to correct problems disclosed in the audit report and what effect such action(s) may have had. ISSAI 4000.232 states, 'The auditor shall decide to follow up on opinions/conclusions/recommendations of instances of non-compliance in the audit report when appropriate.'

It should be noted that the follow-up process may not be applicable in all cases and all SAIs. The SAI's mandate, along with the nature of the audit, will determine if a follow-up is relevant. For example, if the SAI has the mandate to conduct a compliance audit of state-owned enterprises or public sector undertakings, the SAI may conduct follow-up audits of these entities.

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 on the previously reported instances of non-compliance would vary with the nature of the subject matter, the non-compliance identified and the audit's particular circumstances. The follow-up process facilitates the effective implementation of corrective actions. It provides useful feedback to the audited entity, the report users and the auditors in planning future audits. Follow-up serves different purposes for the three parties:

For the responsible party	Demonstrates the audited entity's effectiveness in addressing the issues. One is to encourage an appropriate response to audit findings on the part of the auditee or other responsible entities. If an auditee has acted to overcome problems found during an audit, it is appropriate for the SAI to recognise that fact. If, on the other hand, the auditee has not acted in response to the audit, it is also appropriate for the SAI to disclose that the problem(s) persist.
For the intended user	Provides an update on what has been achieved by the responsible party and the existing gaps, if any.
For the auditor	To assess the effectiveness of its audit. Another purpose of audit follow-up is to lay the foundation for future audit work. If previously disclosed problems are believed to have been resolved, subsequent audit work in that area may require only minimal testing to confirm that the problem no longer persists. If the problem has not been overcome, further audit work may be warranted to establish the nature and significance of the problem, to evoke a more appropriate response from the auditee.

What to follow up

Follow-up focuses on whether the audited entity has adequately addressed the matters raised in a specific audit report.

The auditors generally follow up on the:

- Recommendations in the audit report
- Issues raised by intended users; for example, the legislature, 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 has complied with all the necessary directives.

When to follow up

The decision as to when to follow up would be based on several factors. If the audit was a one-off attestation engagement, then follow-up may not be necessary. However, if auditors come out with significant deviations having implications for the citizens, even if the audit engagement is a one-off, its results should be followed up. If the engagement is 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 and yet still ensure that the follow-up is relevant to the intended users. The auditor would exercise professional judgment in this regard. Some SAIs may, depending on the frequency of an audit engagement, conduct follow-up procedures while performing current audits.

How to follow up

SAIs may have established policies and procedures for conducting follow-up. The auditor may prepare an audit plan identifying the resources to be used, the recommendations and audit findings to be examined and the timeframe in which to complete the follow-up.

Some audit procedures that were used during the initial audit engagement may be applicable during the follow-up. The auditor should assess the 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.

The SAI may decide, based on the results of the follow-up, to continue monitoring the audited entity's implementation measures, or it may take the decision to undertake an entirely new audit engagement. In audits carried out regularly, the follow-up procedures may form part of the subsequent year's risk assessment.

DOCUMENTATION AND QUALITY MANAGEMENT OF COMPLIANCE AUDIT

CHAPTER 8

AUDIT DOCUMENTATION

This chapter explains the documentation and working papers of a compliance audit as required by the ISSAIs and the relevant good practices. Proper documentation throughout an audit – from the planning to the reporting stages – forms the basis of a high-quality audit, which will have the desired credibility among the users.

In the audit process, auditors gather evidence and organise it in folders, either in paper or in electronic form. However, often an auditor asks, 'Exactly what do I have to document?' The ISSAIs answer this question to assist the auditor in documenting with the required working papers. Part C of this Handbook identifies the documentation and quality control measures needed in different phases of the audit with the suggested working paper templates. This chapter further describes how the auditor can arrange for adequate documentation to ensure the audit's overall quality.

The ISSAIs provide direction regarding the content, sequence and format of the audit documentation. ISSAIs leave the form of the documentation up to the professional judgment of the auditors and the SAI. Often, the auditors need to be innovative in the documentation to support their audit conclusions. This chapter elaborates on the purpose and elements of documentation and the components of the working papers.

8.1 ISSAI REQUIREMENTS FOR DOCUMENTATION

ISSAI 4000.89 states, '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.'

AUDIT DOCUMENTATION INCLUDES AS APPROPRIATE (ISSAI 4000.90):

An explanation of the subject matter of the audit.

A risk assessment, audit strategy and plan, and related documents.

The methods applied and the scope and time period covered by the audit.

The nature, the time and extent of the audit procedures performed.

The results of the audit procedures performed, and the audit evidence obtained.

Evaluation of the evidence forming findings, conclusions and recommendations.

Judgments made in the audit process, and the reasoning behind them.

Communication with and feedback from the audited entity.

Supervisory reviews and other quality control safeguards undertaken.

Documentation needs to be sufficient to demonstrate how the auditor defined the audit objective, subject matter, criteria and scope, as well as the reasons why a specific method of analysis was chosen. For this purpose, documentation needs to be organised to provide a clear and direct link between the findings and the evidence that supports them (ISSAI 4000.91).

Specifically related to the audit planning stage, the documentation kept by the auditor needs to contain (ISSAI 4000.92):

a. The information required to understand the entity being audited and its environment, which enables the assessment of the risk.

b. The evaluation of the materiality of the subject matter.

c. The identification of possible sources of evidence.

The auditor needs to adopt appropriate procedures to maintain the confidentiality and safe custody of the audit documentation. The auditor retains it for a period sufficient to meet the needs of the legal, regulatory, administrative and professional requirements of record retention and to enable the conduct of audit follow-up activities (ISSAI 4000.93).

Documenting the critical decisions made is essential to demonstrating the independence and impartiality of auditors in their analysis. 'The existence of sensitive issues demands the documentation of the relevant facts considered by the auditor in choosing a particular course of action or in taking a certain decision. In this way, the actions and decisions are explained and transparent' (ISSAI 4000.94).

'In the context of SAIs with jurisdictional powers, documentation needed to provide proposals of personal liability is outside the scope of this professional standard' (ISSAI 4000.95).

According to the standards, the essential aspects of documentation and working papers are:

Purpose of documentation	Elements of documentation	Organisation of documentation	Documentation at audit stages	Maintaining confidentiality

These aspects are described below.

8.2 PURPOSE OF DOCUMENTATION

ISSAI 4000.90 states that the purpose of documentation is to:

- Enhance the transparency of the work performed.
- Enable an experienced auditor with no previous connection to the audit to understand matters arising from the audit.

It makes significant audit tasks more manageable and helps the audit supervisor and the reviewer provide their review comments. The process of preparing and reviewing audit documentation contributes to the quality of an audit. Audit documentation serves to:

- Provide support for the auditors' report.
- Assist the auditors in conducting and supervising the audit.
- Assist the quality reviewer in the review of audit quality.

Quality review of the audit

The audit team, team supervisors, managers, audit quality reviewers and peer reviewers are the primary users of the audit working papers. Looking at it from a user's point of view, the auditor needs to think about what the reviewers would want to see and what requirements they would want the audit team to comply with. For a compliance audit, the benchmark is the requirements of ISSAI 4000.

The ISSAIs require the auditors to maintain audit documentation in such a manner that an experienced auditor will be able to follow and understand. A qualified auditor is an individual (whether internal or external to the SAI) who possesses the competencies and skills that would have enabled him/her to conduct the audit. These competencies and skills include an understanding of:

The audit process	Standards and legal requirements	The subject matter	Audited entity environment
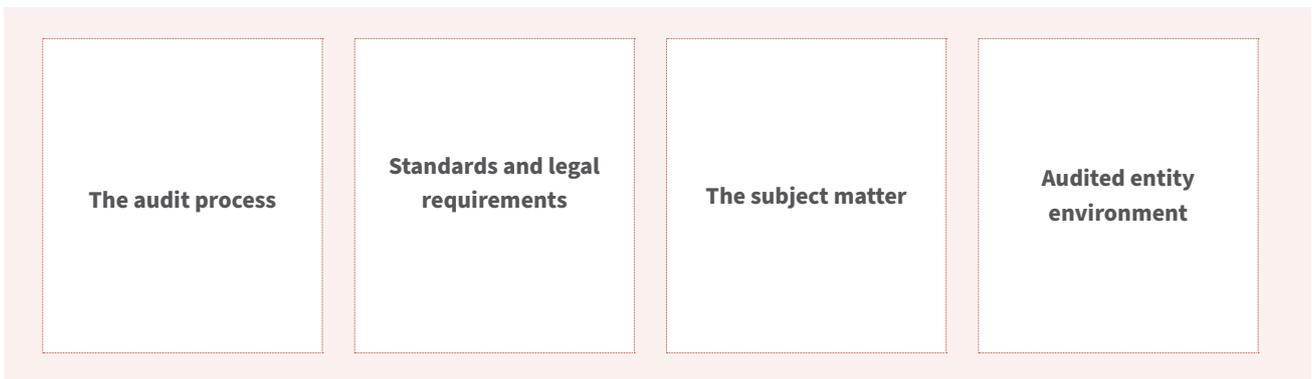
Auditors need to document adequately at every stage of the audit process. Proper documentation helps reviewers to understand what was done, how it was done and why it was done.

Generally, the SAI prepares a standardised set of working papers (as part of audit documentation)

and ascertains what makes them compliant and satisfactory to the supervisor or reviewer. Setting clear expectations regarding documentation and communicating that to its staff will significantly facilitate the quality review process for both auditors and reviewers.

8.3 ELEMENTS OF DOCUMENTATION

The auditor's documentation of evidence regarding identified or suspected non-compliance with authorities may include, for example, copies of records or documents, and 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 concerning compliance audit criteria used in the audit. Auditors will develop and maintain documents that will clearly show that the work was performed.

In determining the nature and extent of the documentation for a compliance audit, auditors may consider the:

Nature	of the auditing procedures performed
Risks	of material non-compliance and auditors' response to the assessed risks
Extent	to which professional judgment was applied (in making decisions)
Materiality	of the evidence obtained against the criteria

As mentioned above, documentation should be sufficiently detailed to enable an experienced auditor, with no prior knowledge of the audit, to understand the:

- Relationship between the subject matter, criteria and audit scope

- Risk assessment

- Audit strategy and audit plan

- Nature, timing, extent and results of the procedures performed

- Evidence obtained in support of the auditor's conclusion or opinion

- Reasoning behind the matters where the auditor exercised professional judgment

- Related conclusions

8.4 COMPONENTS OF WORKING PAPERS

Based on the standards and best practices, the 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 and conclusions
→ Two-way cross-references

THE WORKING PAPER IS:
→ Neat and legible
→ Referenced to the audit programme
→ Understandable without further explanation

IN THE WORKING PAPERS:
→ Calculations are verified
→ Source documents are included as necessary
→ If a document was produced by the entity, it is written on the working paper
→ A review has been indicated and all points were cleared

Source, purpose, procedures, results and conclusions in the working paper

The source, purpose, procedures, results and conclusions should be included on the first page of each unique working paper. Each element should answer the following:

SOURCE	PURPOSE	PROCEDURES	RESULTS	CONCLUSION
→ Where did the auditor get the evidence on the working paper?	→ What question does this working paper seek to answer?	→ What did the auditor do on this working paper?	→ What did the procedures yield?	→ What is the answer to the questions posed in the purpose?
→ Who gave it to the auditor?	→ Why was this working paper created, and why was this work done?	→ What procedure did the auditor use?	→ What were the results of applying the procedure?	→ Was the step satisfied?
→ Which evidence did the auditor look at?	→ What step does it satisfy?	→ What were the detailed steps and procedures the auditor performed?		→ What did the auditor do with any issues found?
→ Where is the evidence and how can the auditor get to it again?				→ Did the auditor take the issues to a finding?

This information is helpful to an audit supervisor or reviewer, as without these elements the supervisor or reviewer has to make assumptions while reviewing the working papers. The auditor needs to make it easier for the reviewer to reach the conclusions and guide them to follow the process smoothly.

The linkage among the elements is also essential. When the linkage is appropriately established, the purpose and conclusions match, and the procedures and results also match. This demonstrates clarity of thought and supports logical conclusions made by the auditor. In most cases, the audit findings matrices (explained in Chapter 7) cover these elements in a compliance audit.

8.5 ORGANISATION OF THE WORKING PAPER DOCUMENTATION

According to the ISSAIs, documentation needs to be organised in a way that provides a clear and direct link between findings and evidence that supports them. It is the auditor who determines how to do it, following existing systems or practices in the SAI. The auditor may have prepared numerous working papers supporting the audit, but for the reviewer or supervisor to understand and analyse, the auditor needs to explain and systematically organise them. Using a summary memo may facilitate this process.

Summary memo

The summary memo can also be called a lead sheet, a conclusions form or a top memo, based on the SAI practice and norms. The memo summarises a group of working papers. Note that the SAI might also have components in the summary memo that differ from those described here.

The summary memos will assist the supervisor or the reviewer in completing the review process efficiently and effectively. Besides that, preparing these memos requires the auditors to articulate their judgments clearly and to document the decisions made while performing the audit, which makes it easier to recognise the logical connection among the 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:

Example: Summary memo	
Audit Objective	In an audit of a purchasing department, after gathering the information and assessing the risks, the auditor decides that the objective is to determine whether the purchasing department complies with required purchasing policies.
Sub-objectives	Under the objective, there are three sub-objectives to determine: → Are purchases of equipment exceeding $9000 conducted in accordance with policy? → Are purchasing procedures established by the entity in accordance with policy? → Are professional contracts awarded in accordance with policy?
Working papers	The auditor will prepare a set of working papers to support each sub-objective and will use **letters** to designate the groups of working papers, like: 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 A1, A2, A3, etc., explain 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:
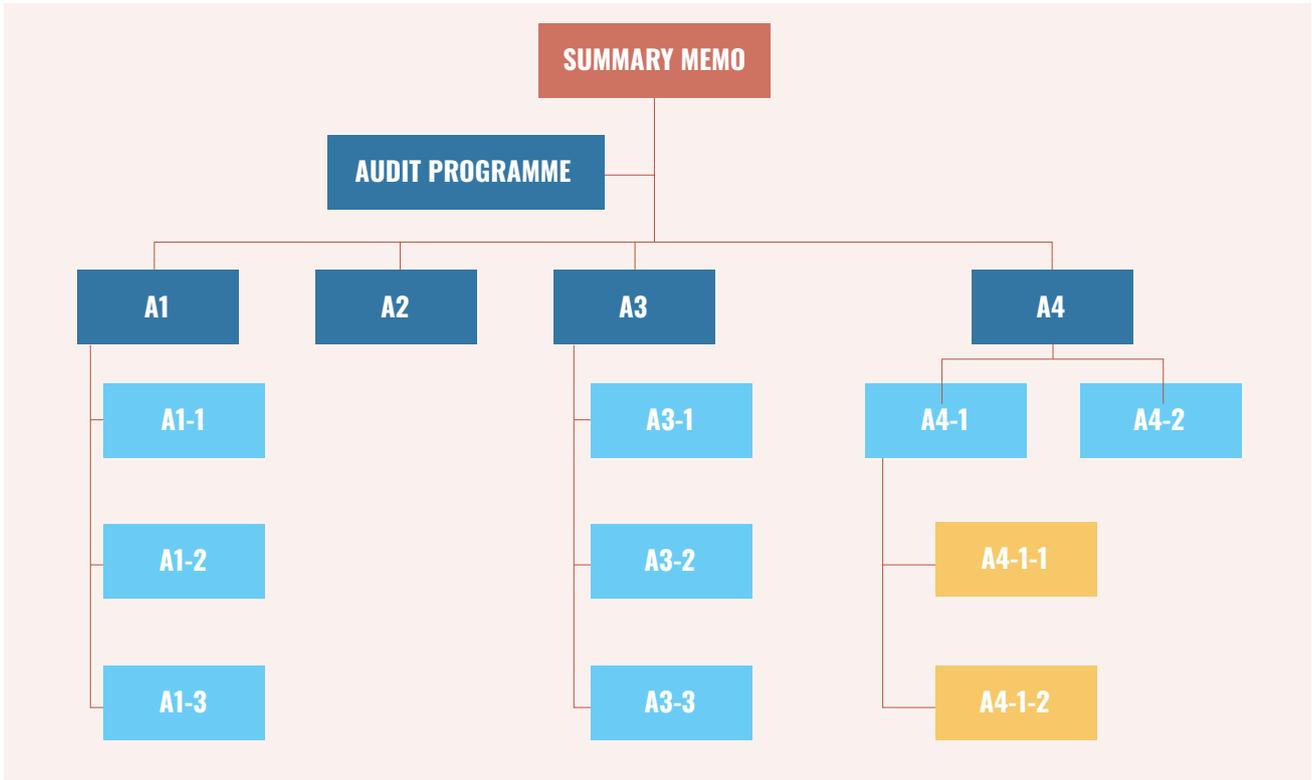
There can be a 'meta' or master summary memo that summarises working paper series A, B and C and speaks to the overarching audit objective: 'Does the purchasing department comply with significant policies?' The auditor can prepare a summary memo for each audit procedure. The working paper series A-4 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.

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.

Example: Working paper format	
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 the programme steps in the area decided, which called on us to: → Reiterate step 1 → Reiterate step 2 → Reiterate step 3
Results	We noted several significant items of non-compliance: → Summarise results of step 1 → Summarise results of step 2 → Summarise results of step 3
Conclusion	The purchasing department did not comply with the purchasing policy section XX regarding purchases of equipment exceeding $9000. In particular, the department allowed the same person to initiate, approve and receive equipment purchases over $9000. This issue has been developed into a finding for the report.

The summary memo can be:

A SOURCE OF 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.

DETAILED OR 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.

INCLUDE WORKING PAPER CONTENTS AND DOCUMENT

→ 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
→ Evidence of supervisory review

Although the standards do not require maintaining a summary memo, it may be considered a good practice for the auditor that will facilitate the work of the reviewer. Auditors could consider the audit findings matrices to cover part of the documentation requirements in the detailed and supporting working papers.

8.6 DOCUMENT RETENTION

Some SAIs may have policies and procedures consistent with their laws and auditing standards to maintain documentation of their work. Documentation retention policies ensure that relevant records are available for use for a certain number of years after an audit. These policies and procedures usually describe:

- Documents covered in their scope
- Form in which the documents would be kept or archived
- Period for which the documents would be retained
- How these documents can be accessed when needed

The auditor should check whether the SAI has policies and procedures for document retention and if they are adequate or not. In the case of inadequacies, the SAI may consider strengthening its policies and procedures with sufficient requirements for the retention of audit documentation.

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. Auditors should familiarise themselves with applicable legislation regarding the retention of documentation.

8.7 CONFIDENTIALITY AND TRANSPARENCY ISSUES

SAIs need to ensure that auditors comply with the ethical requirements to maintain the confidentiality of information gathered during the audit documentation. The auditor should maintain such confidentiality unless the entity authorises expressly 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 identified and treated as such, while at the same time granting access as appropriate. It is therefore vital for the auditor to become familiar with the SAI's policies and procedures addressing confidentiality. SAI procedures might include the types of audit documentation to be considered confidential and the types of audit documentation to be made available to the public.

SAIs should clearly define lines of responsibility for authorising disclosure of audit documentation and routines for making such information available if required. Furthermore, auditors may have additional statutory duties related to confidentiality. These responsibilities may be based on the SAI's mandate or legislation related to official secrets or privacy. Such legislation, for example, could relate to audits of defence, health, social services or tax agencies.

Auditors familiarise themselves with the particular local requirements related to confidentiality by which they are bound. Auditors also familiarise themselves with any legislation that grants public access to audit correspondence. This type of communication 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. In the public sector, the entities might be required by law to respond to the requests received from outside parties to have access to the audit documentation. The third-party attempts can be especially sensitive as they try to obtain information indirectly from the SAI when it is unable to get it 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 generally referred to the audited entity. In situations where auditors consider granting access to audit documentation, they usually consult with relevant parties (such as the audited entity to whom the request relates) before disclosing the information.

In some environments, the SAI contracts out some of its auditing responsibilities to private-sector auditors. The acceptance of such appointments typically requires the contracted auditor performing the work to acknowledge that the audit documentation may be subject to inspection by the SAI. The audit documentation may also be subject to investigation by the agencies that have statutory rights of access to information relevant to the auditor's duties.

QUALITY MANAGEMENT AT THE ENGAGEMENT LEVEL

ISSAI 140 (Revised) establishes the organisational requirements for setting up a System of Audit Quality Management (SoAQM) within a SAI. At the systemic level, the SAI is responsible for developing policies and procedures that enable it to:

- Set quality objectives,
- Identify and assess quality risks,
- Design and implement appropriate responses to those risks, and
- Establish proactive monitoring, remediation, and evaluation processes to ensure the continuous effectiveness of the system.

The SAI's System of Audit Quality Management consists of the following eight interrelated components:

1. SAI's risk assessment process
2. Governance and leadership
3. Relevant ethical requirements
4. Acceptance, initiation, and continuance of engagements
5. Performing engagements and issuing audit reports
6. SAI resources
7. Information and communication
8. Monitoring and remediation process

The effectiveness of the SAI's SoAQM ultimately depends on how well it is applied at the individual audit engagement level. The engagement team, led by the audit supervisor or director, is responsible for implementing the SAI's quality objectives and addressing quality risks in each audit.

Support for Implementation of SoAQM

The IDI's SoAQM Playbook provides practical guidance for SAIs in establishing and implementing their System of Audit Quality Management in accordance with ISSAI 140 (Revised).

9.1 LINK BETWEEN ORGANISATIONAL AND ENGAGEMENT-LEVEL QUALITY MANAGEMENT

Decisions made at the organisational level directly influence quality management at the engagement level—for example, determining the level and nature of review procedures to be applied in specific audits.

ISSAI 4000, paragraphs 52-61, sets out the auditor's responsibilities for managing quality at the engagement level. Quality management is not a separate process but is embedded within the audit process itself.

The table below illustrates how the components of the SAI's SoAQM translate into quality management responsibilities at the engagement level.

SoAQM Component	Quality Management Responsibilities at the Engagement Level
SAI's risk assessment process	→ Implement the SAI's responses to quality risks applicable to the audit engagement (e.g., enhanced review for higher-risk audits). → Identify and implement additional responses for engagement-specific quality risks not covered by SAI-level policies. → Communicate any new or emerging engagement-level quality risks back to the SAI to inform future risk assessments and policy updates.
Governance and leadership	→ The audit supervisor/director, designated by SAI leadership, takes overall responsibility for managing and achieving quality on the engagement. → Ensure active involvement and oversight throughout the audit process.
Relevant ethical requirements	→ Demonstrate understanding of relevant ethical requirements, including independence, integrity, and objectivity. → Evaluate and document any potential threats to independence or ethical compliance at the start of the engagement and apply appropriate safeguards. → Ensure team members comply with ethical requirements and address any identified threats.
Acceptance, initiation, and continuance of engagements	→ Apply SAI policies and procedures for engagement acceptance and continuance. → Implement safeguards for high-risk or mandated audits where specific concerns have been identified.
Performing engagements and issuing audit reports	→ Direct, supervise, and review the work and documentation of audit team members. → Ensure sufficient and appropriate audit evidence is obtained to support conclusions. → Confirm that the audit report is appropriate and not dated until all required quality procedures are completed. → Conduct necessary consultations on significant matters. → Cooperate with engagement quality reviews as required by SAI policy. → Resolve any differences of opinion in accordance with SAI procedures.
SAI resources	→ Ensure that sufficient and appropriate resources are available for the engagement. → Verify that the audit team collectively possesses the necessary competence and expertise to perform the audit. → Where resource constraints exist, document compensating quality measures (e.g., enhanced supervision or post-engagement peer review).
Information and communication	→ Maintain effective communication within the audit team and with relevant stakeholders. → Communicate to the SAI information relevant to the design, implementation, or operation of the SoAQM (e.g., engagement acceptance issues, resource needs, monitoring results). → Communicate audit results to the audited entity and other stakeholders, as appropriate.
Monitoring and remediation process	→ Understand the implications of the SAI's monitoring and remediation process for the engagement. → Apply lessons learned from deficiencies identified in other audit engagements. → When selected for review, cooperate fully with reviewers to facilitate the monitoring process.

Note: While ISSAI 4000 has not yet been revised to reflect changes in the quality management standards, the quality management responsibilities at the engagement level for the respective SoAQM components are derived from the relevant audit best practices.

9.2 ENSURING QUALITY AT THE ENGAGEMENT LEVEL

At the engagement level, the audit supervisor or director should establish specific quality measures to ensure that each audit is performed to a high standard.

High-quality audits are those that:

- Comply with professional standards and applicable laws and regulations,
- Result in an auditor's report that is appropriate in the circumstances, and
- Provide value through relevant, reliable, and credible findings.

The level of review applied depends on the nature, complexity, and risk of the engagement, as defined in the SAI's SoAQM.

9.3 LEVELS OF REVIEW

Complex or high-risk audits may require multiple levels of review, such as:

- First-level review: Detailed review by the audit team leader.
- Second- and third-level reviews: Higher-level reviews by the audit supervisor and audit director.

For smaller or less complex audits—particularly those conducted by a single auditor—multi-level reviews may not be practical. In such cases, the SAI should adopt alternative quality measures, such as:

- Close supervision by the audit director or supervisor,
- Assignment of auditors with appropriate competence and experience, and
- Implementation of peer reviews within the audit division.

When such alternatives are used, the audit director/supervisor should document the compensating measures to demonstrate how quality management objectives were achieved.

9.4 ENGAGEMENT QUALITY REVIEW (EQR)

Where required by SAI policy or in response to identified quality risks, an Engagement Quality Review (EQR) may be conducted to provide an objective evaluation of the significant judgments made and conclusions reached by the audit team.

The purpose of the EQR is to enhance the credibility of the audit report, strengthen professional scepticism, and reinforce the robustness of the SAI's quality management system.

Key requirements include:

- The EQR must be completed on or before the date of the auditor's report.
- The Engagement Quality Reviewer must be objective and independent from the audit team.
- The EQR is mandatory for audits of listed entities or those specifically required by regulation or SAI policy.

9.5 MONITORING AND REVIEW OF ENGAGEMENTS

When an audit engagement is selected for review under the SAI's monitoring and remediation process, the review provides valuable insights into the design, implementation, and operation of the SoAQM at the engagement level.

Reviews typically assess:

- Compliance with professional standards and SAI methodologies,
- The appropriateness of the auditor's report, and
- Whether the audit contributes value and upholds public trust.

The SAI may select audit engagements or audit directors/supervisors as the sampling unit for review. Using audit directors/supervisors as the sampling unit offers several advantages:

- Reinforces accountability and responsibility for quality outcomes,
- Ensures that remedial actions influence all engagements under a specific director/supervisor,
- Allows flexibility when engagement assignments change,
- Enables focused causal analysis and targeted remedial actions, and
- Simplifies follow-up on corrective measures.

Results from these reviews should be analysed and communicated to identify root causes of deficiencies, promote organisational learning, and refine the SAI's policies and procedures. This feedback loop supports continuous improvement in audit quality across the SAI.

The SoAQM Playbook provides tools to assist engagement supervisors/ team leaders in discharging their review responsibilities.

EXHIBITS AND APPENDICES

NOTE: This section includes the working paper templates, as exhibits, and appendices as referenced in the respective chapters of the Handbook. The templates are designed to facilitate the application of the compliance audit ISSAI requirements in practice. Please note that the working paper templates are suggestive, not prescriptive, for appropriate audit documentation. SAIs may need to modify the working paper templates and make them consistent with the SAI's mandate and audit practice, and align them with their current working papers.

Exhibits for Chapter 4:
The SAI's annual work plan for coverage of compliance audit

Exhibit 4.1: Documenting a potential audit task

Exhibit 4.2: Establishing the annual or multi-annual work plan

Appendix 4-A: Categorisation of entities based on risk value

Appendix 4-B: Differing tasks of the auditor in different types of compliance audit

EXHIBIT 4.1: DOCUMENTING A POTENTIAL AUDIT TASK

ISSAI requirement: ISSAI 4000.64

Audit task assessed by		Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

Potential Audit Tasks		
Organisation unit:	Title of task:	Reference:
Link to SAI strategic priority:		
I – Audit field/area		
Main activities:		
Legal framework:		
Financial and other information:		
Roles and responsibilities:		
II – Reasons for the audit		
Risks		
Public and stakeholder interest	Relevance: Materiality:	
Potential added value (including impact, timeliness and coverage)	Previous audits: Timeliness:	
III – Audit organisation		
Audit question (main question and possible sub-questions) or what could be assessed by the audit:		
Audit criteria (or sources for criteria):		
Main sources of audit evidence:		
Audited bodies:		
IV – Remarks		
Feasibility (possible difficulties in the audit/auditability issues..):		
Estimated audit resources:		
Use of existing audit findings:		
Yes ☐		
No ☐		
V – Team members		

Process guide to complete the audit task documentation template

The objective of the template	To document the process of identification of potential audit tasks. There can be different audit tasks identified by different teams in the SAI. This process needs to be repeated for each audit task identified to enable management to agree on a list of audit tasks. The supervisor or management will address the defined tasks in the SAI-level overall planning for a compliance audit.
ISSAI requirement	ISSAI 4000.64
Guide	Consider the explanation provided in section 4.2 of chapter 4, along with this process guide. On the top row, write the linkage with the SAI strategic priorities. This may come from the SAI strategic plan, which has identified the key priority areas on which the SAI will focus during its strategic planning period. If there is no apparent link with the strategic plan, but the team feels that the topic needs to be considered, write the reason for it. <table><tr><td>**Row I**</td><td>Refers to the main activities of the audit field or area; legal, financial and other relevant information; and who is responsible for the area. This will give an overview of the area to be considered.</td></tr><tr><td>**Row II**</td><td>The critical risks are perceived at this point from the field. Also, from public and stakeholder interest, or from any potential added value, including impact, timeliness and coverage. Materiality, by nature, is covered at this stage of SAI-level planning as well.</td></tr><tr><td>**Row III**</td><td>Refers to how the audit would be organised. At this point, it is not required to be precise; the tentative audit questions could be as-sessed, along with possible audit criteria, potential sources of audit evidence and the entities under the audit.</td></tr><tr><td>**Row IV**</td><td>The conceivable difficulties in the audit. Auditability, audit resources and possible use of existing audit findings. This will assist manage-ment in deciding whether it should be included in the plan.</td></tr><tr><td>**Row V**</td><td>Include the details of the team members who proposed the tasks for audit.</td></tr></table>
Review	A person senior to the auditor may review the proposal, keeping in mind the SAI context with pragmatism. This could be documented in the template. It will be based on the SAI structure and the form of the audit teams. The reviewer signs off on the proposal and sends it to the management or the supervisor.
Conclusion	The audit supervisor and management are to conclude whether the task proposed has the potential for audit. This process will assist management in aligning the strategic priorities set by the strategic plan and in achieving the planned goals.

EXHIBIT 4.2: ESTABLISHING THE ANNUAL OR MULTI-ANNUAL WORK PLAN

ISSAI requirement: ISSAI 4000.64

Plan prepared by Assessed by		Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

Annual Plan Period: (............)							
Planned Tasks and Resources							
	Description	Total person-week for the entire task	Total person-week for the planning period	Costs (travel, experts, etc.)	Planned start date	Planned end date	Comments
Non-audit tasks	Example: Annual planning						
	Task 1						
	Task 2 etc.						
	Non-audit tasks total						
Mandatory audit tasks	Task 1						
	Task 2 etc.						
	Mandatory tasks total						
Selected audit tasks	Task 1						
	Task 2 etc.						
	Selected tasks total						
Support functions	Example: Legal services						
	IT services, etc.						
	Support total						
Total resources							

Conclusion

Annual and multi-annual audit tasks and corresponding resources have been prepared considering the above.

(Signature)   (Signature)

Name: Reviewer:

Date: Date:

Process guide to complete the annual or multi-annual work plan

The objective of the template	The objective is to prepare a work plan that includes all the SAI's tasks and to guide how the SAI can identify resources for the selected audit tasks in compliance audits.
ISSAI requirement	ISSAI 4000.64
Guide	The audit plan period is mentioned at the top. Planned tasks are covered in the rows, and resources required are in the columns. Rows are explained below. Resource columns include person week, cost and timeline. These are covered along with the tasks in rows below:
	Row 1 — Write all non-audit tasks that the SAI conducts. These can be the SAI's annual plan, administrative work, training, other consultation work, specific tasks allocated by the stakeholders unrelated to audit, etc. For each non-audit task, complete the respective row considering the resources columns, e.g., person weeks required, costs and timeline. Once all tasks are recorded with resources, add the columns in the 'total' row for all non-audit jobs.
	Row 2 — Similarly, write all mandatory audit tasks the SAI is required to conduct under its legal mandate each year. These could include financial audit, performance audit, compliance audit and other audit requirements mandated by the legislation. Complete the resources column for each task and calculate the total resources of all mandatory assignments.
	Row 3 — The selected audit task row should be filled in a similar manner. For each task chosen, complete the columns with person weeks, costs and timelines. Calculate the total resources required for the selected tasks.
	Row 4 — Complete the resources required for all support functions of the SAI. These include IT, legal, advisory, external training, etc. Add the rows for each service to get the full picture of resources required to provide support functions.
	Row 5 — Determine the total resources required by the SAI to conduct all activities or tasks. From here, it would be evident what resources the SAI has and what it would need to complete the mandatory, non-audit tasks and support functions. Deduct all these from the total resources, and the remaining resources can be allocated to the selected audit tasks.
Overall conclusion by the audit team member	Based on the information gathered in the table and the analysis of the resources, the resources available for the selected tasks are determined and submitted for approval.
Review by supervisor	The supervisor reviews and sends it to SAI management for consideration in future audit assignments for the teams.

APPENDIX 4-A: CATEGORISATION OF ENTITIES BASED ON RISK VALUE[90]

Audited entities are classified as apex auditable entity, audit unit and implementing units. Audit units are based on delegation of powers, functional autonomy and operational significance. Audited entities are categorised as high-, medium- and low-risk entities based traditionally on the budget and expenditure levels. The government database on the expenditure of the entities facilitates the application of the risk analysis framework.

Assessment of inherent risk: Expenditure is categorised in the accounts of all entities under 70 different primary heads of expenditure by all audited entities. These 70 primary heads of expenditure in accounts are regrouped under the following seven broad classes of expenditures:

Expenditure of each audited entity is identified and assessed against seven inherent risk parameters on a 1–5 scale.

Broad classes of expenditure:
I. Personnel services and benefits
II. Administrative expenses
III. Contractual services and supplies
IV. Grants
V. Other expenditure
VI. Acquisition of capital assets and capital expenditures
VII. Accounting adjustments

No.	Inherent risk factor	Remarks	Risk score (1 – 5)
1	**Estimation**	Transactions and decisions involving estimation have a higher inherent risk.	
2	**Discretion**	Transactions involving discretionary powers have an inherent risk of misuse of such powers.	
3	**Complexity in the transaction**	Transactions like capital acquisitions and project execution involve complexity and, therefore, have a higher level of inherent risk.	
4	**Transfer of funds**	Some entities only transfer funds to implementing agencies and do not implement projects or programmes and have low risk.	
5	**Involvement of private agencies**	Private agencies engaged in programme delivery may have interests which lead to higher inherent risk.	
6	**Human resources**	Adequate due diligence may suffer in entities having an acute workforce shortage, leading to higher inherent risk.	
7	**Direct public dealing**	Entities having direct public dealings have relatively higher inherent risk on account of external influence, etc.	
		The inherent risk for primary expenditure	Risk score /35

Based on the inherent risk score of each class of primary head of expenditure under the entity, the entity's total inherent risk value is calculated by aggregating the inherent risk value of all the classes of primary expenditure of that entity and multiplying the same by actual expenditure.

Assessment of control risk: Entities having a weak control environment will have higher control risk. The control risk is assessed through four parameters:

→ Expenditure and related controls

→ Technology-related controls

→ Internal and external audit outputs

→ Other factors

Each parameter has sub-parameters, for a total of 100.

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[90] Based on the presentation by SAI India at the XV Compliance Audit Subcommittee meeting, 9–10 October 2018, Luxembourg

Class of expenditure	Name of the class of the primary head of expenditure	Inherent risk score	Actual expenditure	Risk-weighted expenditure
I	Personnel services and benefits	R1	E1	R1*E1
II	Administrative expenses	R2	E2	R2*E2
III	Contractual services and supplies	R3	E3	R3*E3
IV	Grants	R4	E4	R4*E4
V	Other expenditure	R5	E5	R5*E5
VI	Acquisition of capital assets	R6	E6	R6*E6
VII	Accounting adjustments	R7	E7	R7*E7
	Inherent risk value =			**Grand total**

Control risk factor	Risk score	Control risk factor	Risk score
Expenditure and related controls	(1 – 5)	Internal/external audit	(1 – 5)
Budget procedure and control		Internal audit and inspection	
Increase in expenditure		Quality of record maintenance	
Reported cases of fraud, etc.		Audit observations	
Idling of funds / Pending utilisation certificates		Assessment from performance audit reports and evaluations	
Technology-related controls	(1 – 5)	Other factors	(1 – 5)
Direct transfer of benefits to beneficiaries		Assessment based on data analytics	
Linking of beneficiaries to a unique ID		Quality control mechanism	
Use of e-tendering in procurement		Human resources shortage	
Online monitoring of the programme		Media reports	
Online delivery of services			
Public financial management system			
Use of remote sensing/Geographic Information Systems			
IT controls assessment based on IT audit			
Control risk = Total control risk score / 100			

Risk value and categorisation of entities

After computation of inherent and control risks, the risk score of the audited entity can be determined as:

The risk score of the entity =
   (Total inherent risk score of the entity in monetary value) ✖ (Control risk score of the entity)

Audited entities are categorised as high, medium and low risk based on the risk score. Periodicity of audit and composition of audit team are decided based on the level of risk categorisation.

Risk categorisation of the audited entity

No.	Categorisation	Ceiling risk in US$
1.	High risk	3.5 million
2.	Medium risk	70 000 to 3.5 million
3.	Low risk	Below 70 000

APPENDIX 4-B: DIFFERING TASKS OF THE AUDITOR IN DIFFERENT TYPES OF COMPLIANCE AUDIT

Audit stages	Reasonable assurance (RA)		Limited assurance (LA)	
	Direct reporting – RA	Attestation engagement – RA	Direct reporting – LA	Attestation engagement – LA
PLANNING	The auditor selects the subject matter and produces subject matter information.	The responsible party presents subject matter information on which the auditor then gathers sufficient and appropriate audit evidence.	The auditor selects the subject matter and produces subject matter information.	The responsible party presents subject matter information on which the auditor then gathers sufficient and appropriate audit evidence.
	More extended procedures in risk assessments, understanding the entity and environment, and evaluation of internal control.	More extended procedures in risk assessments, understanding the entity and environment, and evaluation of internal control.	Less extended procedures in risk assessments, understanding of the entity environment and in the evaluation of internal control.	Less extended procedures in risk assessments, understanding of the entity environment and the evaluation of internal control.
	The three components of the audit risk model (inherent, control and detection risks) may be used.	The auditor has to cover the three components of the risk model.	The three components of the audit risk model (inherent, control and detection risks) may be used.	The auditor has to cover the three components of the risk.

Audit stages	Reasonable assurance (RA)		Limited assurance (LA)	
	Direct reporting – RA	**Attestation engagement – RA**	**Direct reporting – LA**	**Attestation engagement – LA**
GATHERING AUDIT EVIDENCE	A combination of different audit techniques is important.	A combination of different audit techniques is important.	It is possible to conclude based on the analytical procedures and inspection.	It is possible to conclude based on the analytical procedures, substantive testing and inspection.
		Substantive testing must always be included.	Analytical procedures and inspections are sufficient.	Substantive testing, analytical procedures and inspections are sufficient.
	The auditor gathers sufficient and appropriate audit evidence to conclude whether the subject matter complies in all material respects with identified suitable criteria.	The auditor gathers sufficient and appropriate audit evidence to conclude whether the subject matter complies in all material respects with identified suitable criteria.	The procedures are limited compared with what is necessary for a reasonable assurance engagement.	The procedures are limited compared with what is necessary for a reasonable assurance engagement.
EVALUATING EVIDENCE AND FORMING CONCLUSION	The conclusion is expressed in the form of findings, answers to specific audit questions, recommendations or opinions.	The auditor provides assurance either through standardised opinions or conclusions. An opinion is normally used.	The conclusion is expressed in the form of findings, answers to specific audit questions, recommendations or opinions.	The auditor provides assurance either through standardised opinions or conclusions. An opinion is normally used.
	The audit conclusion expresses the auditor's view that the subject matter is/is not compliant in all material respects with the applicable criteria.	The auditor's conclusion or opinion expresses the auditor's view that the subject matter information is/is not in accordance with the applicable criteria.	The conclusion conveys that nothing has come to the auditor's attention that the findings are not in compliance with the audit criteria.	The conclusion or opinion conveys that nothing has come to the auditor's attention, and the findings are not in compliance with the audit criteria.

Audit stages	Reasonable assurance (RA)		Limited assurance (LA)	
	Direct reporting – RA	Attestation engagement – RA	Direct reporting – LA	Attestation engagement – LA
REPORTING AND FOLLOW-UP	Report structure in ISSAI 4000.210	Report structure in ISSAI 4000.218	Report structure in ISSAI 4000.210	Report structure in ISSAI 4000.218
	The auditor needs to implicitly state whether the conclusion is given with limited or reasonable assurance.	The auditor provides assurance by making a clear statement of the level of assurance.	The auditor needs to implicitly state whether the conclusion is given with limited or reasonable assurance.	The auditor provides assurance by making a clear statement of the level of assurance.
	The auditor can provide assurance either through (a) conclusions which explicitly convey the level of assurance or (b) explaining how findings, criteria and conclusions were developed.		The auditor can provide assurance either through (a) conclusions which explicitly convey the level of assurance or (b) explaining how findings, criteria and conclusions were developed.	
			A limited assurance report conveys the limited nature of the assurance provided.	A limited assurance report conveys the limited nature of the assurance provided.

Exhibits for Chapter 5:
Planning a compliance audit

EXHIBIT 5.1: AUDIT STRATEGY

ISSAI requirement: ISSAI 4000.13

Entity name	
Audit period	

Audit strategy matrix prepared by		Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

No.	1	2	3
	Elements of the audit strategy	Description	Comments
1	Characteristics of the audit		
2	The audit objective		
3	The audit's subject matter, scope and criteria		
4	The entities covered by the audit		
5	The type of engagement		
6	The level of assurance to be provided		
7	Composition of the audit team		
8	Quality control mechanisms for the audit		
9	Communication with the auditee and those charged with governance		
10	Reporting responsibilities		
	Other significant matters, if any		

Process guide to complete the template for the audit strategy

The objective of completing the template	The objective of this working paper template is to prepare an overall audit strategy detailing the elements of the strategy and to see how each item will impact planning and conducting the audit, and at the reporting phase of the audit.	
ISSAI requirement	ISSAI 4000.137	
Guide	Column 2	Describe based on the decisions made on each element of the strate-gy mentioned in column 1.
	Column 3	Provide comments if the auditor thinks the strategic elements will have any impact on planning and the conducting phase of the audit
Conclusion	The audit team leader and supervisor need to conclude that adequate consideration has been given to all significant areas affecting the audit, and an appropriate strategy has been put in place to deal with the matters that were likely to influence planning and to perform the audit. Audit strategy working paper document should be updated continuously.	
Evidence from the preparer and the reviewer	The table indicating the name of a person who prepared and documented the material and the reviewer's name needs to be completed at the end.	

EXHIBIT 5.2: UNDERSTANDING THE ENTITY AND ITS ENVIRONMENT

ISSAI requirement: ISSAI 4000.131

Entity name	
Audit period	

	Prepared by	Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

Questions	Description
The entity's legal framework	
1. The authorising legislation for the entity and the activities authorised by the legislation	
2. The regulations issued under authorising legislation and their effect on the entity's operations	
3. How does the entity comply with the legal framework?	
4. Is there any provision in the regulations regarding the rules and regulations for financial management?	
The entity's objectives and strategies	
5. The entity's objectives	
6. The key policies and strategies to achieve the objectives	
The entity's organisation and governance	
7. The entity's governance structures	
8. The operational structure, organisation chart and management arrangements	
9. The financial, human resources and other resources	
The entity's business processes and operations	
10. What is the nature of the entity's operations? The entity's core functions.	
11. How the significant audit areas relate to the entity's operations	
12. The types of programmes, functions or projects managed by the entity	

Questions	Description
13. The process narratives provide an overview of the functions and operations of the entity or the subject matter	
14. The critical business process maps, flowcharts of the operations	
15. The operational risks related to the entity's objectives and strategies that may result in material non-compliance	
The entity's financial management systems	
16. Financial reporting framework the entity used for financial reporting	
17. Entity's budgeting process	
18. Entity's accounting system, reporting requirements and deadline of reporting	
19. Internal audit and external audit function of the entity	
The entity's performance measures	
20. How is the entity's performance measured and reviewed?	
21. What are the entity's performance reporting requirements?	
22. Are there performance targets that may result in management actions increasing the risk of non-compliance?	

List of significant risks affecting the entity (linked to the inherent risks)

Process guide to complete the template for understanding the entity and its environment

The overall objective of completing the template	The objective of this audit working paper template is to establish and document an understanding of the entity and its environment relevant to an audit. ISSAI 4000.131 requires the auditor to assess the risk of non-compliance through understanding the entity and its environment.
	[Note: The template could be adapted to the subject matters, e.g., for a programme, a particular operation of an entity, a contract or procurement.]
ISSAI requirement	ISSAI 4000.131
Guidance	The auditor needs to understand the entity and its environment to assess the risk of non-compliance in its operations and financial activities.
	Based on the list provided in the template above, the auditor can gather a general understanding of the entity, taking into account both internal and external factors. The auditor must understand the entity's core business. While documenting the understanding of the entity and its environment, the auditor needs to bear in mind the risk related to the entity (business risks or entity risk) that may occur during its operations and that may result in material non-compliance in the entity.
	Consider the list of source documents provided in the table below as a possible source for finding and documenting the information required.
Conclusion	The team should ensure that this documentation is linked to assessing the risk of material non-compliance (inherent risks) and assessing the control environment.
Evidence from the preparer and the reviewer	The table indicating the name of a person who prepared and documented the material and the reviewer's name needs to be completed at the end.

Potential sources of documents to understand the entity:

No.	Documents
1	Mandate, roles, and responsibilities of the organisation
2	Draft financial statements
3	Approved budget of the government, projects and NGOs
4	Plan documents
5	List of major activities carried out during the period to be audited
6	Project organisation
7	Accounts of grants and borrowings
8	Project documents
9	List of laws, rules and regulations that are relevant and applicable
10	Loans and grant agreements
11	Consolidated budget fund accounts
12	Other sources of funding for the entity
13	List of major agencies incurring expenditure
14	Minutes of review meetings
15	Important correspondence files
16	The standard financial reporting requirement
17	Fund flow procedures, including reimbursement and repayments
18	Past audit reports and internal audit reports
19	List of bank accounts and statements
20	Financial rules and regulations
21	Procurement rules

EXHIBIT 5.3: UNDERSTANDING THE INTERNAL CONTROLS AND CONTROL ENVIRONMENT

ISSAI reference: ISSAI 4000.134

Entity name	
Audit period	

	Prepared by	Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

[Note: The fundamental concepts of the internal control framework are formulated as 17 principles associated with the five components of the framework.[91] The questions below are based on these principles, which are relevant to all entities and need to be present, functioning and operating together in an integrated manner to have an effective system of internal control.]

Questions on the internal control components	Description
Control environment	
1. How does the entity ensure its commitment to integrity and ethical values?	
2. What mechanisms or bodies exist to assume the oversight responsibilities for the entity management's design, implementation and conduct of internal control?	
3. How do the entity's organisational structure and assignment of authority and responsibility contribute to maintaining an appropriate control environment?	
4. How do the entity's human resources policies and procedures demonstrate commitment to having the competence and the required level of skills and expertise?	
5. How does the organisation enforce accountability on the overall conduct and hold individuals accountable for their internal control responsibilities?	
Risk assessment	
6. Does the entity have a risk assessment process and consider the significant risks to the achievement of its objectives?	

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[91] https://www.coso.org/Documents/COSO-CROWE-COSO-Internal-Control-Integrated-Framework.pdf

Questions on the internal control components	Description
7. How does the management use the risk assessment process to effectively identify, analyse and respond to the risks of non-compliance?	
8. How does the entity management consider the potential for fraud in assessing the risks to the achievement of its objectives?	
9. How does the management identify and analyse the changes that could significantly impact the internal control system, and the management override of internal controls?	
Control activities	
10. How does the entity select and develop control activities that contribute to the mitigation of risks to the achievement of its objectives?	
11. Does the entity ensure that the general control activities are designed effectively and operating as intended to address the risks over use of technology?	
12. How does the entity, through its policies that establish what is expected and procedures that put the policies into action, ensure the selection, development and deployment of appropriate control activities in significant risk areas?	
Information and communication	
13. How does the entity obtain or generate and use relevant, quality information to support the functioning of internal control?	
14. How does the entity internally communicate information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control?	
15. How does the entity communicate with external parties regarding matters affecting the functioning of internal control?	
Monitoring	
16. How does the entity select, develop and perform ongoing and separate evaluations to ascertain whether the components of internal control are present and functioning?	
17. How does the entity evaluate and communicate internal control deficiencies on time to those parties responsible for taking corrective action, including the senior management and the governing body, as appropriate?	

Process guide to complete the template for understanding the internal control

The objective of completing the template	This template provides an understanding of the five interrelated components of an entity's internal control system. The auditor's role within this system focuses on the internal controls over the entity's operations, financial reporting and the processes in place.	
ISSAI reference	ISSAI 4000.134	
Guide	Control environment	The control environment is the set of standards, processes and structures that provide the basis for carrying out internal con-trol across the organisation. The senior management establishes the tone at the top regarding the importance of internal control and expected standards of conduct.
	Risk assessment	Risk assessment involves a dynamic and iterative process for identifying and analysing risks to achieving the entity's objectives, forming a basis for determining how risks should be man-aged.
	Control activities	Control activities are the actions established by policies and pro-cedures to help ensure that management directives to mitigate risks related to the achievement of objectives are carried out. Control activities are performed at all levels of the entity and at various stages within business processes, and throughout the technology environment.
	Information and communication	Information is necessary for the entity to carry out internal con-trol responsibilities in support of the achievement of its objec-tives. Communication occurs both internally and externally and provides the organisation with the information needed to carry out day-to-day controls. Communication enables personnel to understand internal control responsibilities and their importance to the achievement of objectives.
	Monitoring activities	Ongoing evaluations, separate evaluations or some combination of the two are used to ascertain whether each of the five components of internal control, including controls to affect the principles within each segment, is present and functioning. Findings are evaluated and deficiencies are communicated on time, with serious matters reported to senior management and the board.
Conclusion	The audit team concludes on the significant areas of the control environment under evaluation.	
Evidence from the preparer and the reviewer	The team and the reviewer, usually the audit supervisor, should sign off on this document to ensure that the work done by the team has been reviewed and documented.	

EXHIBIT 5.4: ASSESSMENT OF FRAUD RISKS

ISSAI requirement: ISSAI 4000.58

Entity name	
Audit period	

	Prepared by	Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

[The checklist below is not inclusive of all questions needed to assess fraud risks in an organisation. It might require follow-up questions that depend on the answers to previous questions. Accordingly, auditors may use this as a start to create their tools and to brainstorm to identify the fraud risks that could apply to the entity or subject matter.]

Questions	Description
1. Does the entity have a fraud governance structure in place that assigns responsibilities for fraud investigations?	
2. Does the entity have a fraud policy in place?	
3. Has the entity identified laws and regulations relating to fraud in jurisdictions where it operates?	
4. Does the entity's fraud management programme include coordination with, if one exists, its internal audit function?	
5. Does the entity have a fraud hotline?	
6. Has responsibility for fraud detection, prevention, response and awareness been assigned within the entity?	
7. Does entity management promote fraud awareness and training within the organisation?	
8. What processes have been put in place for identifying and responding to the risks of fraud in the entity?	
9. Are periodic fraud awareness and training programmes provided to all employees?	
10. Are any automated tools available to those responsible for preventing, detecting and investigating fraud?	
11. Has the entity management identified the types of potential fraud risks in its areas of responsibility?	
12. Has entity management incorporated appropriate controls to prevent, detect and investigate fraud?	
13. Does entity management have the appropriate skill sets in place to perform fraud investigations?	
14. Does entity management periodically assess the effectiveness and efficiency of fraud controls?	
15. Are fraud investigation work papers and supporting documents appropriately secured and retained?	

Process guide to complete the template for the assessment of fraud risks at the audit planning stage

The objective of completing the template	The objective of this template is to have information regarding fraud risk as part of an overall understanding of the entity and control environment.
ISSAI requirement	ISSAI 4000.58
Guide	The fraud risk assessment team identifies potential fraudulent schemes using brainstorming, management interviews, analytical procedures and review of prior frauds. During this process, the fraud risk assessment team reviews the organisation's activities and schemes relevant to the industry, geography and programmes, always considering the essential characteristics of fraud (pressure, opportunity and rationalisation), asking:
	→ Where are the opportunities for fraud?
	→ What is the level of pressure that management is under that would lead it to override internal controls?
	→ Are there any consequences if management fails to reach goals?
	Specific fraud areas should be identified without consideration of existing or the effectiveness of internal controls. The evaluation considers whether the fraud could be committed by an individual alone or requires collusion among employees or external persons.
	The auditor may consider the following factors while prioritising fraud risks:
	→ Financial impact
	→ Impact on the organisation's reputation
	→ Potential criminal or civil actions
	→ Regulatory non-compliance
	→ Integrity and security over data
	→ Loss of assets
	→ Location and size of operations and units
	→ Entity culture
	→ Management and employee turnover
	→ Liquidity of entity assets
	→ Volume and size of transactions
	→ Outsourcing
Conclusion	The audit team concludes on the potential fraud risks to be documented in the risk register.
Evidence from the preparer and the reviewer	The team and the reviewer, usually the audit supervisor, sign off on this document to ensure that the work done by the team has been reviewed and documented.

EXHIBIT 5.5: SETTING MATERIALITY AT THE PLANNING STAGE

ISSAI requirement: ISSAI 4000.92

Entity name	
Audit period	

	Prepared by	Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

1	2	3	4	5	6
Benchmark	**Threshold**	**Materiality % used**	**Population amount**	**Materiality amount**	**Revised materiality amount**
Payment amount	1 to 5%	x%	Xxxx	xxxx	xxxx
Revision	1 to x%	x%	Xxxx	xxxx	xxxx

Setting quantitative materiality (if subject matter includes transactions, financial information)

Justification for benchmark used (how the total amount is derived)

Justification for the percentage used

Reason for revised materiality

Setting qualitative materiality

Materiality by nature

Materiality by context

Process guide to complete the template for setting materiality at the planning stage

The objective of the template	The objective of completing this working paper template is to determine materiality for planning and performing the audit, and this is carried out as a part of the overall audit strategy. The materiality determined at the planning stage can be revised as the audit progresses.
ISSAI requirement	ISSAI 4000.92
Guide	The purpose of materiality is to identify the audit questions, based on the risk assessment, and ensure that any non-compliance below the materiality level will not affect the conclusion and will not affect the purpose for which the reports are used by users.

Column 1	Select an appropriate benchmark in determining the planning materiality for the subject matter under consideration. While choosing this benchmark, the auditor needs to consider whether this item is critical to the users.
Column 2	Determine the threshold of materiality. The limit will depend on the SAI's policy, and it could be, for example, between 0.5% to 2% or 1% to 5%. This may also depend on the type of benchmark chosen from the audit's overall subject mat-ter.
Column 3	From the given threshold, select a percentage to be applied to the total population value to arrive at the materiality amount. The auditor applies a percentage of the materiality considering the sensitivity of items. The percentage to be ap-plied may be decided as follows: Very sensitive: 1%, sensitive: 2.5%, not sensitive: 5%
Column 4	Record the total population amount of the chosen benchmark derived from the subject matter.
Column 5	Derive the materiality amount by applying the chosen percentage (from Column 3) to the total population amount (Column 4). This is the planning materiality amount for the subject matter if it is a transaction or financial information.
Column 6	To arrive at a revised value, repeat the same process as above. Using professional judgment, the auditor may also simply state the revised materiality amount without having to apply the revised percentage to the total population.

	Recording descriptions related to determining materiality:
	→ Under row 1, record the description for using the chosen benchmark, how the total amount is derived and how it is used as a benchmark.
	→ Under row 2, record the justification; primarily, it is dependent on sensitivity. It may also depend on the nature of the entity and the financial discipline.
	→ Under row 3, record the reason for revising the materiality, to keep track of why the materiality amount was revised and why there was a need to revise the materiality.
	Under qualitative materiality:
	→ Under row 1, record the consideration of materiality by nature that needs to be considered throughout the audit. This particular aspect is crucial in public sector auditing.
	→ Under row 2, record the consideration of materiality by the context that needs to be considered throughout the audit. This is sometimes minor non-compliance, but may have a significant effect.
Evidence from the preparer and the reviewer	The reviewer, usually the audit supervisor, should sign off on this document to ensure that it has been reviewed.

EXHIBIT 5.6: RISK REGISTER

ISSAI requirement: ISSAI 4000.52

Entity name	
Audit period	

Prepared by		Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

No.	1 Risk identified (inherent/control/fraud risks)	2 Link to the area under the subject matter	3 Assessment (High, low, medium)
1.	..		
2.	..		

Process guide to complete the template for risk register

The objective of completing the template	The objective of this working paper template is to record the risks of non-compliance identified while completing the risk assessment process. ISSAI requires the auditor to assess the risks of material non-compliance through understanding the entity and its environment.	
ISSAI requirement	ISSAI 4000.52	
Guide	Overall	The recording of risks in the risk register may take place simulta-neously while determining the inherent, control and fraud risks. During the audit, this risk register can be updated based on new risks identified, without having to go through the whole process again. Risks from the register are elaborated in the planning ma-trix with the audit procedures to be performed.
	Column 1	In this column, the auditor records the risks identified in different areas. While recording these risks, the auditor gets the input from the inherent risks, control risks and fraud risks identified.
	Column 2	The auditor records the relevant areas of the subject matter where the risks are linked.
	Column 3	The risks identified and recorded in the risk register are assessed considering the impact and likelihood, and the auditor's conclusion on the risk is recorded.
Evidence from the preparer and the reviewer	The names of the person who prepared this risk register and the reviewer at the end. The preparer, who could be a team leader or one of the team members, needs to sign off accordingly. The reviewer, usually the audit supervisor, should sign off on this document to ensure that the work done by the team has been reviewed accordingly.	

EXHIBIT 5.7: AUDIT PLAN

ISSAI reference: ISSAI 4000.137, ISSAI 4000.140, ISSAI 4000.149

Entity name	
Audit period	

	Prepared by	Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

[**Note:** The audit plan has the following parts: Part A: Assessment of risk and internal control; Part B: Audit Planning Matrix covering the risks; Part C: Audit schedule covering who and when the audit procedures will be performed. The SAI team can combine the audit strategy and audit plan in one continuous document for approval by the SAI management.]

PART A: Assessment of risks and internal control

1. Assessment of risks

2. Assessment of internal control

3. Result of risk assessment: risk register

4. Materiality assessment

PART B: Audit planning matrix

No.	1	2	3	4	5
	Risks identified (from risk register)	Criteria	Required evidence/ information	Sources of evidence/ information	Audit procedures to perform
1					
2					
3					
4					
5					
6					
..					
..					

PART C: Audit schedule

Audit stages	Planned date	Achieved date	Comments
Audit plan			
Prepared			
Reviewed			
Approved by management			
Audit execution: Field work			
Start			
Completion			
Audit reporting			
Draft report prepared			
Reviewed			
Approved by management			
Audit report issued			

Process guide to completing the template for the audit plan

The objective of the template	This working paper creates the basis for the audit strategy and audit plan document that the audit team will submit to the management for approval.
ISSAI references	ISSAI 4000.137, ISSAI 4000.140, ISSAI 4000.149
Guide	**Part A: Assessment of risks and internal control**

Assessment of risks	The risk assessment process followed. Mention the overall information from the understanding of the entity and the fraud risk identified. These should come from the completed working paper templates.
Assessment of internal control	Write the assessment of overall control risk, based on the results of the understanding of the subject matter and the initial assessment of control risks.
Result of the risk assess-ment	Document the risk assessment results and the assurance required to give reasonable assurance on the subject matter. The risks are listed in the risk register.
Materiality	Describe both quantitative and qualitative aspects of materiality, as applicable, considering the exhibit on materiality.

Part B: Audit planning matrix

Risks identified	Bring all risks of material non-compliance in this column as the audit questions from Exhibit 5.6 on the risk register list.
Criteria	In an audit strategy, all applicable criteria are identified for the subject matter. Here, the specific criteria that the entity should comply with regard to the respective risk in column 1 need to be mentioned.
Required evidence	What evidence or information does the auditor need to answer the audit question regarding the risk of non-compliance against the criteria?
Sources of evidence	Where is the evidence or information available? Write a list of possible sources of evidence for the audit.
Audit procedures to perform	Write what audit procedures the team plans to confirm whether the condition complies with the criteria to answer the question. For example: make inquiries with staff and document discussions, review policies and note non-compliance, for further discussions with the entity.

Part C: Audit schedule

Detail the dates planned for the audit. When the audit is going on, there may be changes, so the 'achieved date' part will have to be filled in later and comments added based on the progress of the audit.

APPENDIX 5-A: QUALITY REVIEW OF AUDIT PLANNING

Purpose	Quality review of audit planning
Reference	Section 5.3

[The review checklist provided below is suggestive. The SAI may already have a quality review mechanism with an agreed list. The SAI team can compare the two and finalise the checklist for the quality review at the planning stage.]

The reviewer, while reviewing the adequacy of audit planning, may consider the following matters:

	Checklist	Review comment
1	Ensuring that planning is carried out following auditing policies, standards, manuals, guidelines and practices of the SAI	
2	Obtaining relevant information regarding laws and regulations that might have a significant impact on the audit objectives	
3	Preliminary investigative audit (an audit that aims to conduct an initial study of specific issues to help prepare the audit plan)	
4	Determining objectives and the scope of the audit	
5	Identification of sources (e.g., media, findings of the auditee's internal audit, inspection and other control bodies) as background for audits	
6	Determining the list of activities for audit	
7	Highlighting of unique problems foreseen when planning the audit	
8	Ensuring that members of the audit team have a clear and consistent understanding of the audit plan	
9	Follow-up is made on issues in previous related audits	
10	Understanding the finance, accounting and other relevant functions of the entity and subject matter	
11	Identification of critical elements of the internal control system of the auditee	
12	Using appropriate analytical procedures	
13	Identification and analysis of relevant ratios and comparative figures	
14	Identification of trends or deviations from predicted amounts	
15	Choice of relevant performance indicators	
16	Assessment of inherent and control risks	
17	Establishment of materiality criteria and thresholds	
18	Preparation of the audit planning matrix with the risks identified	
19	Choice of appropriate experts, if required	
20	Preparation of budget and schedule, assessment of resources necessary, staff requirements and team allocated for audit	
21	Investigation and settlement of queries raised during the review stage	
22	Drawing up, approval, and review of the audit plan by supervisors, if applicable	
23	Other procedures and practices used in the planning phase of an audit	
24	Practices to continuously enhance quality control procedures in the planning phase of the audit	

Exhibits for Chapter 6:
Performing audit procedures, and gathering and evaluating evidence

EXHIBIT 6.1: TESTING THE OPERATING EFFECTIVENESS OF CONTROLS

ISSAI references: ISSAI 4000.144–149

Entity name	
Audit period	

	Prepared by	Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

Step 1: Link from planning to risk, control activities, and test procedures

1	2	3	4	5	6
Control reference number	Risk	Risk reference	Control activity for the risk	Control testing procedures performed	Comments
Link to…	Link to…			Link to…	

Step 2: Test of control procedures performed

1	2	3					4
Sample	Sample reference no.	Item tested in the sample					Conclusion
		Item 1	Item 2	Item 3	Item 4	Item 5	
1							
2							
3							
4							

Overall conclusion on control testing

Process guide to complete the template for testing the operating effectiveness of controls

Objective of the template	The objective of this working paper template is to document the control testing procedures performed by the auditor. The test objective is linked to identified risks; the audit procedure is performed on the samples selected.
ISSAI	ISSAI 4000.144–149
Guide	Step 1: Link the risks from the planning document that were considered for testing and record them in the field provided above. Against this, trace the risks, control activities and control testing procedures identified from the planning document.
	Step 2: Select samples to be tested for one control activity at a time. First, record the control reference number and risk reference number to confirm which control was tested. Record this in the field provided in the template, and then record the details of the samples in the given table.

Step 1: Link from planning to risk, control activities, and test procedures

Column 1	In this column, trace the control activity reference number from the Log of Control Activity or from the RMNC (risk of material non-compliance)/risk register table completed at the planning stage of the audit. Column 1 records the control reference number and thus provides a status of controls being tested.
Column 2	Trace risks identified in the RMNC/risk register table and record them in this column. First, trace the risks assessed as significant.
Column 3	It is optional to trace the name of the risk or the risk reference in this documentation. The risk reference number can be traced from the RMNC/risk register table and recorded in this column.
Column 4	Trace the name of the control activity from the RMNC/risk register table and record it in this column. It should correspond to the control activity reference number recorded in column 1 and the risks traced from the RMNC/risk register.
Column 5	In this column, add a comment on control testing procedures designed at the planning stage from the RMNC/risk register table. This is the work that needs to be performed by the auditor.

Step 2: Test of control procedures performed

Column 1	In this column, record the sample numbers. This indicates how many samples were tested.
Column 2	Document the sample reference number in this column. Typically, it could be a payment voucher or receipt voucher number, a date or similar.
Column 3	In this column, record the details of items tested in that particular sample against the control. Items to be tested in a particular sample will be determined by the control testing procedures designed at the planning stage and by the test objective.
Column 4	Arrive at a conclusion on every sample tested and record it in this column. This will form the basis for arriving at an overall conclusion.

Conclusion on control testing	Based on the controls identified against each risk tested, conclude as to whether the controls put in place are operating effectively. To do so, first record the basis for the conclusion, and then conclude with either of the following statements. 1. The controls were operating effectively. 2. The controls were not operating effectively. This conclusion should then be traced back to the RMNC/risk register table under the column specified as 'Conclusion of control testing procedure' and recorded as either 'Effective' or 'Not effective' against each control testing procedure.
Evidence from the preparer and reviewer	The table indicating the names of the person who prepared and completed this working paper and the reviewer needs to be completed at the end. The preparer could be a team leader or one of the team members, who could then sign off accordingly. The reviewer, usually the audit supervisor, should sign off on this document to ensure that the work done by the team has been reviewed accordingly.

EXHIBIT 6.2: PERFORMING SUBSTANTIVE AUDIT PROCEDURES

ISSAI references: ISSAI 4000.144–149

Entity name	
Audit period	

	Prepared by	Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

Step 1: Link from planning to risk and substantive audit procedures

1	2	3	4
Risk	**Risk reference**	**Substantive audit procedures performed**	**Comments**
Link to…		Link to…	

Step 2: Substantive audit procedures performed

1	2	3					4
Sample	**Sample reference no.**	**Item tested in sample**					**Conclusion**
		Item 1	Item 2	Item 3	Item 4	Item 5	
1							
2							
3							
4							

Overall conclusion on the substantive audit procedures

Completing the template for substantive audit procedures: Suggested process guide

The objective of the template	The objective of this audit working paper template is to document the substantive audit procedures performed by the auditor in the execution phase of the audit to ensure that the work performed by the auditor is documented accordingly. The test objective is linked to the identified risk; the audit procedure is performed on the samples selected.
ISSAI	ISSAI 4000.144–149
Guide	Step 1: Link the risks from the planning document that were considered for testing and record them in the field provided above. Against this, link the risks and the substantive audit procedures identified from the planning document. Step 2: Select samples for testing. Usually, the samples selected for substantive testing are larger than those for control testing. Therefore, the auditor needs first to record the risk reference number, so that it is quite clear which risk will be addressed by performing substantive audit procedures. The particulars or items to be tested in the given sample would depend on the test objective, and what needs to be tested should be drawn from the substantive audit procedures. **Step 1:** Link to the risk and substantive audit procedures from planning After recording the risks to be tested, proceed to complete the table with four elements. The auditor should first focus on significant risks, and design and perform substantive audit procedures that are responsive to such risks.

Column 1	Link risks identified from the RMNC/risk register table and record in this column. First, link the risks assessed as significant.
Column 2	The risk reference number can be linked from the RMNC/risk register table and recorded in this column for ease of reference while documenting substantive audit procedures performed.
Column 3	In this column, link the substantive audit procedures designed at the planning stage from the RMNC/risk register table. This is the work that needs to be performed by the auditor.
Column 4	Add a comment here on the process and the outcome. The purpose is to ensure that the test objective is maintained consistently to arrive at an appropriate conclusion based on substantive audit procedures performed.

Step 2: Substantive audit procedures performed

Document the substantive audit procedures performed that are responsive to assessed risks of material non-compliance. Link risk reference and record in the given field.

Column 1	In this column, record the sample numbers. This indicates how many samples were tested.
Column 2	Document the sample reference number in this column. Typically, it could be a payment voucher or receipt voucher number and date.
Column 3	In this column, record the items tested in that sample. Items to be tested in a sample will be determined by the substantive audit procedures designed and the test objectives determined in the planning stage.
Column 4	In this column, record the conclusion arrived at on every sample tested. This will form the basis for arriving at an overall conclusion.

Conclusion on substantive audit procedures	To arrive at an overall conclusion, first establish the basis of the conclusion. This can be derived by summarising the conclusion for each sample under column 4.

The overall conclusion should then be linked back to the specific risks in the risk register so that auditors will know which risks have actually resulted in non-compliance. From that, constructive recommendations can be suggested.

Any exceptions observed while performing the substantive audit procedures on each sample selected for testing should be linked to the observation list in the completion and review stage of the audit to deal appropriately with management and to evaluate the impact on the objective and subject matter. |
| **Evidence from the preparer and the reviewer** | The table indicating the names of the person who prepared and completed this working paper and the reviewer needs to be completed at the end. The preparer could be a team leader or one of the team members, who could then sign off accordingly.

The reviewer, usually the audit supervisor, should sign off on this document to ensure that the work done by the team has been reviewed accordingly. |

EXHIBIT 6.3: AUDIT FINDINGS MATRIX

ISSAI requirement: ISSAI 4000.179

Entity name	
Audit period	

Prepared by		Signature	Reviewed and approved by	Signature
Name:				
Designation:				
Date:				

1. Risk/audit question: ....

2. Finding

i. Audit criteria	ii. Condition/evidence	iii. Cause	iv. Effect

3. Conclusion: ....

4. Recommendation (if applicable): ....

Completing the template for the audit findings matrix: Suggested process guide

The objective of the template	The objective of completing this working paper template is to facilitate systematically preparing the audit findings. The auditor needs to fill in this template for each risk. Based on the information gathered in the template, the auditor will prepare the individual narrative finding (the team can follow the SAI's finding format). Claims made by the auditor in the narratives in the template should be supported by the required documentation with references (evidence). This will facilitate the quality review process during the audit and quality assurance after the audit.
ISSAI	ISSAI 4000.179

Guide	**Row 1**	**Audit questions** or risks identified at the planning phase, which have reference to the risk register. For each risk/audit question in the register, an audit planning matrix is completed, based on the audit procedures performed for the risks; this table is completed separately for each risk.
	Row 2	**Findings**, which have four elements:
	i. Audit criteria	Authorities, rules or regulations governing the particular entity, events or situation are used to determine the answer to the risk; that is, whether it is compliant or not.
	ii. Condition/ evidence	Condition refers to the existing situation, identified and documented during the audit: What the auditor found in the audit, the existing situation in the entity, whether it deviates from set criteria and results of the collection of evidence using different methods, techniques and procedures. The evidence is linked to the criteria. The auditor analyses the difference between the criteria (what should be) and the condition (what is there) by assessing the evidence of the condition found against the criteria. Often, there are several items of evidence that form a finding.
	iii. Cause	The cause is the reason for the difference between the condition and the criterion. If there is non-compliance, what is the cause? It could be ignorance of the rules in force or the overriding of a management decision. The cause (or the root cause) will be the basis for the recommendations. To reliably identify the causes of the existing situation, the auditor may require using appropriate data analysis methodologies.
	iv. Effect	The effect is the consequence of the difference between the condition and the criterion, i.e. the non-compliance. The effect indicates the seriousness of the situation encountered and determines the intensity of corrective action. What is the effect or consequence of the non-compliance or deviation with regard to loss or other damage to the entity?
	Row 3	**Conclusion**: Based on the analysis, whether the risk under audit is or is not compliant with the respective criteria.
	Row 4	**Recommendations** should come from the root cause of the non-compliance determined. It may be that not all findings have recommendations. When suggesting a recommendation, it is good practice to discuss with the entity the logic and probability of its implementation. This will enhance the recommendation's prospects for implementation.

	Documentation:
	All columns will have statements, which are based on the auditor's professional judgment. All these statements need to be substantiated with sufficient and appropriate evidence and required documentation. The decisions made by the auditor, the application of professional judgment and the decision-making process need to be documented. The work performed and analysis made of the data or information gathered to formulate a conclusion also need to be documented appropriately.
Evidence from the preparer and the reviewer	The table indicating the names of a person who completed the template and who reviewed it is completed at the end. It is usually the team leader who would sign off as part of quality control. The reviewer, usually the audit supervisor, should sign off on this document to ensure that it has been reviewed.

APPENDIX 6-A: QUALITY REVIEW OF AUDIT FIELD-WORK

Purpose	Quality review of audit field-work
Reference	Section 6.6

[The review checklist provided below is suggestive. The SAI may already have a quality review mechanism with an agreed list. The SAI team can compare the two and finalise the checklist for the quality review at the audit field-work stage.]

The reviewer, while reviewing the adequacy of audit field-work, may consider the following matters:

	Checklist	Review comment
1	The audit is carried out in accordance with the auditing standards, manuals, guidelines and practices of the SAI.	
2	Auditors have a sound understanding of techniques and procedures such as inspection, observation, enquiry and interviewing to collect audit evidence.	
3	All phases of the audit have been carried out as planned and approved.	
4	Explanations are available for non-performance of any significant areas in the audit plan.	
5	Appropriate approval exists for significant deviations that have taken place from the approved audit.	
6	Staff resources used for audit are in line with those planned in terms of time, the grade of staff and expenses entailed.	
7	Appropriate audit techniques and audit procedures were used to fulfil each audit objective in order to provide for effective audit evidence.	
8	Computer-assisted audit techniques (CAATs) were used as appropriate.	
9	Appropriate tests were used for evaluating the reliability of internal controls.	
10	Appropriate analytical procedures were used, and the reliability, independence and quality of relevant supporting data were assessed.	
11	Sampling methods were used according to the SAI's manuals and sound statistical methods.	
12	All tests of transactions are related to audit objectives, adequately explain the nature and extent of audit work and provide an overall conclusion as to the results of audit work.	
13	Audit steps and procedures were designed to obtain sufficient and appropriate evidence.	
14	A full investigation was made of all queries raised during the audit.	
15	There are adequate working papers in respect of: evaluation of internal control systems audit of routine procedures tests of controls analytical review substantive tests, and audit of computer-based applications.	
16	Working papers are appropriately cross-referenced.	
17	Audit completion checklists are comprehensive and have been completed, approved and duly evidenced.	

Appendix for Chapter 7:
Reporting and follow-up compliance audits

Appendix 7-A: Quality review of audit reporting

APPENDIX 7-A: QUALITY REVIEW OF AUDIT REPORTING

Purpose	Quality review of audit reporting
Reference	Section 7.5

[The review checklist provided below is suggestive. The SAI may already have a quality review mechanism with an agreed checklist. The SAI team can compare the two and finalise the checklist for the quality review at the reporting stage.]

The reviewer, while reviewing the adequacy of audit reporting, may consider the following matters:

	Checklist	Review comment
1	Reporting is in accordance with auditing policies, standards, manuals, guidelines and practices of the SAI.	
2	The form and content of reports are in accordance with established procedures (e.g., title, signature and date, objectives and scope, addressee, legal basis, timeliness).	
3	The terminology used in the report can be easily understood by persons to whom the report is presented, and technical terms are fully explained.	
4	All audit findings have been evaluated in terms of materiality, errors and other irregularities.	
5	All instances of non-compliance, deficiencies and unusual matters have been properly identified, documented and satisfactorily resolved or brought to the attention of a senior SAI officer, if applicable.	
6	The final audit report covers all areas representing the objectives of the audit, and explanations are provided for omissions.	
7	Observations and conclusions in the report are supported and well documented to ensure completeness, accuracy and validity of working papers.	
8	All evaluations and conclusions are soundly based and supported by competent, relevant and reasonable audit evidence.	
9	Only sufficiently material audit findings are included in the main audit report.	
10	The report is timely, comprehensive, performed by suitably qualified staff, appropriately documented and adequately incorporates the audit opinion.	
11	Letters of weakness, queries and management letters are submitted to the auditee in due time.	
12	Receipt of relevant and timely replies to SAI reports and other correspondence is ensured.	
13	Replies are carefully studied.	
14	All findings, conclusions and recommendations contradicted by the auditee are duly evaluated.	
15	Material relevant comments by the auditee are referred to in the audit report, if applicable.	
16	Relevant significant events occurring following completion of the audit are taken into account in the final audit report.	
17	All significant fraud or other irregularities are reported to the appropriate authorities.	
18	Permanent audit files have been updated to take into account the results of the audit.	
19	Material items requiring subsequent follow-up by the SAI have been duly identified, recorded and taken into account.	

Compliance Audit ISSAI Implementation Handbook, Version 1

INTOSAI Development Initiative (IDI)

INTOSAI

IDI

DEVELOPMENT INITIATIVE