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United States Government Accountability Office
Washington, DC 20548

May 30, 2008

International Auditing and Assurance Standards Board
International Federation of Accountants
545 Fifth Avenue, 14th Floor
New York, New York 10017

Subject: International Auditing and Assurance Standards Board (IAASB)
December 2007, Exposure Draft: ISAE 3402, *Assurance Reports on Controls at a
Third Party Service Organization*

This letter provides the U.S. Government Accountability Office's (GAO) comments on the IAASB's proposed International Standard on Assurance Engagements (ISAE) 3402. Overall, we support the proposed standard.

The Board has asked respondents to answer specific questions and to comment on other matters in the exposure draft. We provide the requested answers and comments in this letter and recommend specific wording changes in the related attachment.

Request for Specific Comments

Question 1.

The IAASB would welcome views on the proposal that the ISAE be written for application to assertion-based engagements. In particular, the IAASB would welcome any views on whether there are situations in which it would not be possible or practicable for management of the service organization to provide an assertion.

Response/Comment:

We support the IAASB's decision to write the proposed standard for application to an assertion-based engagement, where the service organization's management confirms, in a statement made available to users, certain information about the design and, for type B reports, the operating effectiveness, of the service organization's controls. An assertion-based engagement is preferable to a direct reporting engagement, in which all relevant information is included in the service auditor's assurance report and there is no management assertion. Also, including in the report management's acknowledgement of its responsibility for the design and, for type B reports, the operating effectiveness, of controls serves as an important accountability mechanism, clearly informing report users that management is responsible for controls.

We recommend modifying the requirements in paragraph 12 on engagement acceptance and continuance to allow for situations when an examination of internal control is required by law or regulation and the service auditor cannot decline the engagement. Although paragraph A3 of the proposed standard provides guidance for the auditor to follow in these circumstances, we believe it is important to alert auditors in the standard itself that such laws or regulations may exist, especially in the public sector. We provide specific wording changes to paragraph 12 in the attachment to this letter.

Question 2.

The IAASB would welcome views on the inclusion in the proposed ISAE of a number of requirements based on ISAs dealing with matters such as using the work of the internal audit function, sampling, documentation, and using the work of a service auditor's expert. In particular;

1. Has the IAASB identified all such matters as are relevant?
2. Should these matters be dealt with in proposed ISAE 3402 or in ISAE 3000?

Response/Comment:

1. The proposed ISAE omits an important requirement relevant to controls at service organizations. The service auditor should be required to perform certain procedures to identify the risk that the description of the system is not fairly stated or that stated control objectives will not be achieved due to intentional acts by service organization personnel. This is consistent with user auditor responsibilities for identifying material misstatements in user entity financial statements, whether caused by error or intentional act. It also addresses the risk that financial statements of user entities may be materially misstated as a result of intentional acts by service organization personnel. Both Type A and B reports should address the risk of intentional acts or error at the user organization.

We provide specific wording for this change in proposed new paragraphs to follow paragraph 32 and paragraph A10, respectively, of the attachment to this letter.

2. ISAE 3000 establishes basic principles, and provides guidance to auditors for performing assurance engagements. As such, ISAE 3000 should also include the basic requirements that auditors should follow in performing assurance engagements on matters such as using the work of the internal audit function, sampling, documentation, and using the work of a service auditor's expert. However, until ISAE 3000 is revised, the proposed ISAE 3402 should advise user auditors to refer to relevant International Standards on Auditing (ISAs) for the basic requirements that third party service organization auditors should follow in performing assurance engagements.

Question 3. The IAASB would welcome views on whether ISAE 3000 should be amended with respect to auditor's external experts as outlined above.

Response/Comment:

We recommend that ISAE 3000 be amended to include requirements and guidance on using the work of a service auditor's external experts, as ISAE 3000 establishes the guidance on the basic principles and essential procedures for auditors. Until ISAE 3000 can be revised, we agree that including the requirement with respect to the service auditor's external experts in ISAE 3402 paragraph 26 is appropriate.

Question 4. The IAASB would welcome views on the proposed requirements regarding the minimum elements of suitable criteria.

Response/Comment:

We recommend that the standard on suitable criteria include principles-based attributes of criteria. We provide suggested wording to insert before paragraph 15 describing the four attributes - objectivity, measurability, completeness, and relevance - that should be used to evaluate the criteria used by the service organization. This would make the standard more principles-based and encourage consistency of practice.

Paragraphs 15 through 17, as currently written, contain detail about the scope and application of criteria needed in an assurance engagement for service organizations. The standard should be clarified to indicate that paragraphs 15 and 16 deal with application rather than characteristics of suitable criteria. We provide specific wording changes in paragraphs 15 and 16 of the attachment to this letter.

Question 5. The IAASB would welcome views on whether the description of tests of controls included in a Type B report should include the disclosure of sample sizes determined by the service auditor only when a deviation from controls is found.

Response/Comment:

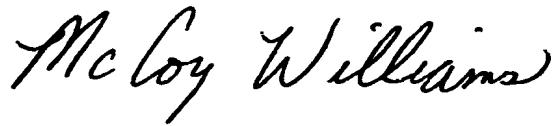
We agree with the IAASB's decision to not require disclosure of sample sizes used by the service auditor unless a deviation from controls is reported. Disclosing the sample size without additional information to put the sample size into proper context may result in users misinterpreting the significance of the sample size as it relates to the audit objectives.

Comments on Other Matters:

- The discussion of modified reports in paragraphs 58 and A30 of the proposed standard provides little guidance for auditors on issuing modified assurance reports on controls at service organizations. To assist auditors and encourage consistency of practice, we recommend including a reference to ISAE 3000, paragraphs 51-53 in ISAE 3402, paragraph A30. We provide specific wording changes in paragraph A30 of the attachment to this letter.
- Without additional context, paragraphs 38 - 41 could be interpreted as a requirement for sampling in assurance engagements to report on controls at service organizations. We recommend revising paragraph 38 of the proposed standard to clarify that the auditor determines whether sampling is appropriate. This will also help clarify that the discussions on attribute sampling and the nature and cause of deviation in paragraphs 39-41 apply to situations when the auditor has determined that audit sampling is an appropriate means of selecting items for testing.

We thank you for considering our comments on these important issues.

Sincerely yours,



McCoy Williams
Managing Director
Financial Management and Assurance

Attachment

cc: Mr. James M. Sylph, Technical Director
International Auditing and Assurance Standards Board

The Honorable Christopher Cox, Chairman
Securities and Exchange Commission

Mr. Kjell Larsson, Public Member
International Auditing and Assurance Standards Board

The Honorable Mark W. Olson, Chairman
Public Company Accounting Oversight Board

Mr. Harold Monk, Chair
Auditing Standards Board

Exposure Draft

December 2007

Comments are requested by May 31, 2008

*Proposed International Standard on Assurance
Engagements*

ISAE 3402, Assurance Reports on
Controls at a Third Party Service
Organization

Proposed Conforming Amendment

Preface to the International Standards
on Quality Control, Auditing, Review,
Other Assurance and Related Services



International Federation
of Accountants

REQUEST FOR COMMENTS

The International Auditing and Assurance Standards Board (IAASB), an independent standard-setting body within the International Federation of Accountants (IFAC), approved the exposure draft, proposed International Standard on Assurance Engagements (ISAE) 3402, “Assurance Reports on Controls at a Third Party Service Organization” for publication in December 2007. This proposed ISAE may be modified in light of comments received before being issued in final form.

Please submit your comments, preferably by email, so that they will be received by **May 31, 2008**. All comments will be considered a matter of public record. Comments should be addressed to:

International Auditing and Assurance Standards Board
International Federation of Accountants
545 Fifth Avenue, 14th Floor
New York, New York 10017 USA

Comments should be emailed to Edcomments@ifac.org. They may also be faxed to +1-212-286-9570 or mailed to the above address.

Copies of the exposure draft may be downloaded free-of-charge from the IFAC website at <http://www.ifac.org>.

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CONTENTS

	Page
Explanatory Memorandum	4
Introduction.....	4
Background.....	4
Significant Matters.....	4
Guide for Respondents.....	9
Exposure Draft	
Proposed International Standard on Assurance Engagements (ISAE) 3402, “Assurance Reports on Controls at a Third Party Service Organization”	11
Proposed Conforming Amendment	
Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services	48

EXPLANATORY MEMORANDUM

Introduction

This memorandum provides background to, and an explanation of, the proposed International Standard on Assurance Engagements (ISAE) 3402, “Assurance Reports on Controls at a Third Party Service Organization.” The International Auditing and Assurance Standards Board (IAASB) approved the proposed ISAE in December 2007 for exposure.

Background

The IAASB commenced this project in 2006 concurrently with a project to revise extant ISA 402.¹ The IAASB recognized the growing use of service organizations by user entities and the need for a service organization to be able to provide user entities and their auditors with a service auditor’s assurance report on its controls. This proposed ISAE will provide the standards for such assurance reports. It is intended to complement proposed ISA 402 (Revised and Redrafted),² in that reports prepared in accordance with proposed ISAE 3402 will be capable of providing appropriate evidence under proposed ISA 402 (Revised and Redrafted).

The IAASB believes that the proposed ISAE will enhance the consistency of auditor performance in relation to assurance reports on controls at third party service organizations, particularly in those jurisdictions that have adopted IAASB standards and have not, to date, had a specific standard on this topic. It is expected that proposed ISAE 3402, in conjunction with proposed ISA 402 (Revised and Redrafted), will enhance the consistency of auditor performance in relation to the audit of the financial statements of user entities.

The proposed ISAE is drafted on the assumption that a service organization has many customers (user entities) and each user entity and its financial statement auditor receive a copy of the description of the system and the service auditor’s assurance report. For this reason, the proposed ISAE assumes a direct relationship between user entities and user auditors, and between service organizations and service auditors, but does not assume any direct relationship between the service auditor and either user entities or user auditors. The proposed ISAE can also be applied, however, to other situations, where a direct relationship between the service auditor and the user entity or user auditor may exist.

Significant Matters

Form of the Standard

The standard has been drafted using the conventions developed for International Standards on Auditing by the IAASB (‘the clarity drafting conventions’). These are currently being applied to ISAs in a project whereby all ISAs will be completed or revised in clarity form by the end of 2008. As part of that project, the “Preface to the International Standards on Quality Control, Auditing,

¹ ISA 402, “Audit Considerations Relating to Entities Using Service Organizations.”

² Proposed ISA 402 (Revised and Redrafted), “Audit Considerations Relating to an Entity Using a Third Party Service Organization,” approved for exposure by the IAASB in December 2007.

Review, Other Assurance and Related Services” (Preface) has been revised to describe the authority of the revised standards, which will all become effective together in 2010.³

The IAASB has not yet applied the clarity drafting conventions to ISAEs – of which there are at present only two: ISAE 3000⁴ and ISAE 3400.⁵ Proposed ISAE 3402, which has been drafted under the clarity drafting conventions, requires the service auditor to comply with ISAE 3000 and well as the proposed standard. The IAASB believes it is appropriate to use the clarity drafting conventions in drafting ISAEs, as it represents IAASB’s view of the clearest way of presenting standards so as to distinguish requirements from guidance and promote consistent interpretation and performance by auditors.

The IAASB has no immediate plans to redraft ISAE 3000 in the clarity form, or to revise that standard, though it acknowledges that this will be necessary at some stage when resources become available. In the meantime, the IAASB believes that because ISAE 3000 is a more general standard establishing the basic principles for the conduct of assurance engagements it is unlikely that practitioners will have difficulty in applying both ISAE 3000 and proposed ISAE 3402 notwithstanding their different forms.

An appropriate conforming amendment is proposed to the Preface as a result of this distinction (see page 49).

Type of Report

The proposed ISAE allows for two types of reasonable assurance reports: Type A, which is confined to opinions on the fairness of the description of the service organization’s controls and on whether those controls were suitably designed for their purpose; and Type B, which additionally includes an opinion, based on tests of the controls, on the operating effectiveness of the controls tested (which may not be all controls described). The proposed ISAE requires that Type B reports should cover a reasonable period, while Type A reports are required to be at a point in time.

There are a number of reasons for the distinction in the time period covered. First, Type A reports are likely to be more common in the initial stages of the operation of a service organization when it is unlikely that there have been significant changes in controls over the period to the date of the report or, where there have been such changes, the more important consideration will be what controls are now in place. A Type A report may also be appropriate when a service organization does not have a sufficient track record with a stable system to make a Type B report feasible, which is the usual circumstance in which a Type A report currently is sought in practice. Secondly, since no tests of controls are undertaken for the purposes of a Type A report, there is no basis upon which a user auditor may choose to rely on the controls at the service organization without further work; there is therefore no clear need for a report that covers a period of time. Thirdly, the provision of a Type A report that covers a period may imply, or may be read as implying, that there is some basis

³ The amended Preface can be accessed at http://web.ifac.org/download/IAASB_Preface.pdf.

⁴ ISAE 3000, “Assurance Engagements.”

⁵ ISAE 3400, “The Examination of Prospective Financial Information.”

for reliance and may therefore be misleading. Consequently, the IAASB considers that there will be neither demand for nor benefit in a Type A report that covers a period of time.

Assertion-based Engagements

The proposed ISAE has been written for application to assertion-based engagements,⁶ where management of the service organization confirms, in a statement made available to intended users that accompanies the description of the system, the matters noted in paragraph 9(j)(ii) of the proposed ISAE for a Type B engagement, and paragraph 9(i)(ii) for a Type A engagement.

The IAASB is of the view that an assertion-based engagement is more appropriate than the alternative (a direct reporting engagement, under which all relevant information is included in the service auditor's assurance report and there is no public assertion⁷) because it includes an explicit acknowledgement, by management of the service organization to the user entities, of its responsibility for the fair presentation of the description of the system, the suitable design of controls and, in the case of a Type B report, the operating effectiveness of controls. Assertion-based engagements are prevalent in some jurisdictions; in others, direct reporting engagements are more common. It should be noted that the nature, timing and extent of the service auditor's procedures would ordinarily be the same regardless of whether the engagement to report on controls at a service organization is an assertion-based or direct reporting engagement. Further, in the case of a direct reporting engagement, a service auditor obtains representations from the management of the service organization that contain confirmations equivalent to the assertions proposed in ISAE 3402. (See Question 1 on page 9.)

Link with International Standards on Auditing (ISAs)

The IAASB is of the view that because the engagement seeks to provide reasonable assurance, and therefore is comparable to a financial statement audit, it would be desirable for the proposed ISAE, taken with ISAE 3000, to cover similar matters and at a similar level of detail to the ISAs to the extent practicable and relevant. Alternative ways to achieve this in the proposed ISAE include replicating or adapting relevant requirements from the ISAs when they are appropriate to the scope of the ISAE; or requiring that all ISAs be applied, adapted as necessary in the circumstances of the engagement.

The IAASB is of the view that it is not appropriate to adopt the approach of requiring all ISAs to be applied, adapted as necessary in the circumstances of the engagement, because to do so would not result in sufficient clarity as to which requirements of the ISAs should be applied or how they ought to be adapted. Therefore, in preparing the proposed ISAE, the IAASB has included a number of requirements based on proposed ISAs dealing with matters such as using the work of the internal

⁶ Assertion-based engagements are contrasted with direct reporting engagements in paragraph 10 of the "International Framework for Assurance Engagements."

⁷ In a direct reporting engagement to report on controls at a service organization, the service auditor would ordinarily obtain a representation from the service organization regarding the matters noted in paragraph 9(j)(ii) of the proposed ISAE for a Type B engagement, and paragraph 9(i)(ii) for a Type A engagement, but that representation would not accompany the description of the system or otherwise be made available to user entities or their auditors.

audit function, sampling, documentation, and using the work of a service auditor's expert. To the extent comments on these proposed ISAs result in changes to the requirements and application and other explanatory material in those standards, the parallel requirements in this ISAE would be conformed.

Further alternatives to this approach might be to amend ISAE 3000, or to draft further ISAEs dealing with such general matters as are likely to be relevant in all assurance engagements.

Auditor's External Experts

With respect to using the work of a service auditor's expert, the Explanatory Memorandum to proposed ISA 620 noted that proposed ISQC 1 (Redrafted) includes a revised definition of engagement team that "specifically excludes 'an auditor's external expert' from the engagement team."⁸ If a similar definition of engagement team were to be adopted in the International Federation of Accountants' Code of Ethics for Professional Accountants (the Code), external auditors' experts, i.e., those who are engaged, not employed, by the auditor, would not be subject to the Code, including its independence requirements. In recognition of this, paragraph 26 of proposed ISAE 3402 includes the following requirements: "the service auditor shall evaluate whether the service auditor's expert whose work is to be used has the necessary ... objectivity for the purposes of the engagement. In the case of a service auditor's external expert, the evaluation of objectivity shall include inquiry regarding interests and relationships that may create a threat to that expert's objectivity."⁹ If the proposed definition of engagement team is ultimately adopted in proposed ISQC 1 (Redrafted) and the Code, it will affect all ISAEs, including ISAE 3000. Therefore, if and when that definition is adopted, the IAASB will consider whether ISAE 3000 should include requirements similar to those in paragraph 26 of the proposed ISAE 3402.

Suitable Criteria

The existence of suitable criteria is a prerequisite for any assurance engagement. For an assurance engagement to report on controls at a service organization, suitable criteria are required for evaluating whether the description of the system is fairly presented, whether the controls are suitably designed and, in the case of a Type B report, whether the controls have operated effectively. To ensure an appropriate level of consistency in the application of the proposed ISAE in relation to the suitability of criteria, the IAASB has specified the minimum elements of suitable criteria.¹⁰ The minimum elements of suitable criteria, for evaluating whether the description of the system is fairly presented, have primarily been adapted from ISA 315 (Redrafted).¹¹

⁸ Proposed ISA 620 (Revised and Redrafted), "Using the Work of an Auditor's Expert;" and proposed International Standard on Quality Control (ISQC) 1 (Redrafted), "Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements," approved for exposure by the IAASB in July 2007.

⁹ Proposed ISAE 3402, paragraph 26.

¹⁰ Proposed ISAE 3402, paragraphs 15-17.

¹¹ ISA 315 (Redrafted), "Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment," paragraph 14(a).

Control Objectives

The IAASB discussed whether to include specimen control objectives in an appendix to the proposed ISAE. It recognized that some may find these helpful. On the other hand, any such objectives would not be comprehensive, and would need to be supplemented (or supplanted) by objectives specific to the services provided by the service organization. The IAASB took the view that any benefit of providing specimen objectives would be outweighed by the risk that they may be inappropriately used on a specific engagement. Those with the necessary skill and experience required to undertake these engagements are expected to have the expertise to identify appropriate control objectives and to assess the completeness of those identified by a service organization.

Description of Tests of Controls

In a Type B report, the service auditor expresses an opinion on the operating effectiveness of controls. That opinion is based on tests of controls. The proposed standard will require that the report include a description of those tests.

The IAASB debated whether to require such disclosure when an opinion is also being given. On the one hand, receipt of a satisfactory opinion might be thought to be all that the user auditor requires. On the other hand, the tests of controls have been conducted on controls that in effect form part of the information systems of the user entity, and therefore of those information systems that form a basis for the financial statements that are subject to audit by the user entity's auditor. Since the report will be used by many user entity auditors who do not in general have the opportunity to instruct the service auditor as to the work to be done, the IAASB considers that it is important for the user auditor both to know that the service auditor is satisfied with the operating effectiveness of controls and to obtain an understanding of the work that has been undertaken to reach that conclusion. This is because the user auditor must form a view as to whether that work is sufficient in the context of the user entity under audit, and how that work relates to the procedures undertaken by the user auditor.

Disclosure of Sample Sizes

The description of tests of controls required to be included in a Type B report does not include the disclosure of sample sizes used by the service auditor unless a deviation from controls is found.¹² This is consistent with current practice in most jurisdictions

The IAASB concluded that disclosure of sample sizes may not provide, on its own, sufficient information to the intended users to understand the judgments made by the service auditor in their determination; therefore, there might be a risk that intended users may misinterpret the significance of different sample sizes as they relate to user entities. The IAASB concluded, on the other hand, that disclosure of sample size when a deviation from controls is found provides intended users with relevant information as to the rate of deviation encountered in the sample. This information assists user auditors in the performance of their risk assessments.

¹² Proposed ISAE 3402, paragraphs 57.

Guide for Respondents

The IAASB welcomes comments on all matters addressed in the exposure draft. Comments are most helpful when they refer to specific paragraphs, include the reasons for the comments, and, where appropriate, make specific suggestions for any proposed changes to wording. When a respondent agrees with proposals in this exposure draft (especially those calling for change in current practice), it will be helpful for the IAASB to be made aware of this view.

Request for Specific Comments

The IAASB would welcome views on the following:

1. The proposal that the ISAE be written for application to assertion-based engagements. In particular, the IAASB would welcome any views on whether there are situations in which it would not be possible or practicable for management of the service organization to provide an assertion.
2. The inclusion in the proposed ISAE of a number of requirements based on ISAs dealing with matters such as using the work of the internal audit function, sampling, documentation, and using the work of a service auditor's expert. In particular, has the IAASB identified all such matters as are relevant? And should these matters be dealt with in proposed ISAE 3402 or in ISAE 3000?
3. Whether ISAE 3000 should be amended with respect to auditor's external experts as outlined above.
4. The proposed requirements regarding the minimum elements of suitable criteria.
5. Whether the description of tests of controls included in a Type B report should include the disclosure of sample sizes determined by the service auditor only when a deviation from controls is found.

Comments on Other Matters

The IAASB is also interested in comments on matters set out below.

- *Special Considerations in the Audit of Public Sector Entities*—Respondents are asked to comment whether, in their opinion, special considerations with respect to public sector entities have been dealt with appropriately in the proposed ISAE.
- *Developing Nations*—Recognizing that many developing nations have adopted or are in the process of adopting the International Standards, the IAASB invites respondents from these nations to comment, in particular, on any foreseeable difficulties in applying the proposed ISAE in a developing nation environment.
- *Translations*—Recognizing that many respondents may intend to translate the final ISAE for adoption in their own environments, the IAASB welcomes comment on potential translation issues noted in reviewing the proposed ISAE.

EXPLANATORY MEMORANDUM

To be considered, responses should be emailed to Edcomments@ifac.org. They may also be faxed to +1-212-286-9570 or mailed to 545 Fifth Avenue, 14th Floor, New York, NY 10017, USA. They should be received by **May 31, 2008**.

PROPOSED INTERNATIONAL STANDARD ON ASSURANCE ENGAGEMENTS 3402
ASSURANCE REPORTS ON CONTROLS AT A THIRD PARTY SERVICE
ORGANIZATION

(Effective for service auditor’s assurance reports covering periods beginning on or after [date])

CONTENTS

	Paragraph
Introduction	
Scope of this ISAE.....	1-6
Effective Date	7
Objectives	8
Definitions	9
Requirements	
ISAE 3000.....	10
Ethical Requirements	11
Acceptance and Continuance	12-13
Assessing the Suitability of the Criteria.....	14-17
Materiality.....	18
Using the Work of an Internal Audit Function	19-25
Using the Work of Service Auditor’s Expert.....	26-31
Obtaining an Understanding of the Service Organization’s System	32
Obtaining Evidence Regarding the Description	33-34
Obtaining Evidence Regarding Design of Controls.....	35
Obtaining Evidence Regarding Effectiveness of Controls	36-41
Written Representations.....	42-44
Other Information	45-46
Subsequent Events	47-48
Documentation.....	49-55
Preparing the Service Auditor’s Assurance Report	56-58
Other Communication Responsibilities	59

Application and Other Explanatory Material

Definitions.....	A1
Ethical Requirements.....	A2
Acceptance and Continuance.....	A3-A4
Assessing the Suitability of the Criteria.....	A5
Materiality.....	A6
Using the Work of an Internal Audit Function.....	A7-A8
Obtaining an Understanding of the Service Organization’s System.....	A9-A10
Obtaining Evidence Regarding the Description.....	A11-A14
Obtaining Evidence Regarding Design of Controls.....	A15-A17
Obtaining Evidence Regarding Effectiveness of Controls.....	A18-A24
Written Representations.....	A25-A26
Preparing the Service Auditor’s Assurance Report.....	A27-A30
Other Communication Responsibilities.....	A31
Appendix 1: Example Management Assertions	
Appendix 2: Example Service Auditor’s Assurance Reports	
Appendix 3: Example Modified Service Auditor’s Assurance Reports	

[Proposed] International Standard on Assurance Engagements (ISAE) 3402, “Assurance Reports on Controls at a Third Party Service Organization” should be read in conjunction with the “Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services.”

Introduction

Scope of this ISAE

1. This International Standard on Assurance Engagements (ISAE) deals with reasonable assurance engagements undertaken by a professional accountant¹ to report on the controls at a third party organization that provides a service to user entities when those controls are likely to be part of user entities' information systems relevant to financial reporting. It complements [proposed] ISA 402 (Revised and Redrafted),² in that reports prepared in accordance with this ISAE are capable of providing appropriate evidence under [proposed] ISA 402 (Revised and Redrafted).
2. The focus of this ISAE is on controls at third party service organizations relevant to financial reporting by user entities. It may also be applied, adapted as necessary in the circumstances of the engagement, for engagements to report on:
 - (a) Controls at a service organization other than those that are likely to be part of user entities' information systems relevant to financial reporting (for example, controls that affect user entities' regulatory compliance, production or quality control).
 - (b) Controls at a shared service center, which provides services to a group of related entities.
3. In addition to issuing an assurance report on controls, a service auditor may also be engaged to provide the following reports, which are not dealt with in this ISAE:
 - (a) A report on a user entity's transactions or balances maintained by a service organization; or
 - (b) An agreed-upon procedures report on controls at a service organization.
4. The "International Framework for Assurance Engagements" (the Assurance Framework) notes that an assurance engagement may be either an "assertion-based" engagement or a "direct reporting" engagement. This ISAE applies to assertion-based engagements.

Relationship with Other Professional Pronouncements

5. The service auditor is required by paragraph 10 of this ISAE to comply with ISAE 3000³ in addition to this ISAE. The Assurance Framework, which defines and describes the elements and objectives of an assurance engagement, provides the context for understanding this ISAE and ISAE 3000.
6. Compliance with ISAE 3000 requires, among other things, that the service auditor comply with the International Federation of Accountants' Code of Ethics for Professional

¹ A professional accountant is defined in the International Federation of Accountants' (IFAC) Code of Ethics for Professional Accountants as an individual who is a member of an IFAC member body.

² [Proposed] ISA 402 (Revised and Redrafted), "Audit Considerations Relating to an Entity Using a Third Party Service Organization."

³ ISAE 3000, "Assurance Engagements Other than Audits or Reviews of Historical Financial Information."

Accountants, and implement quality control procedures that are applicable to the individual engagement.⁴

Effective Date

7. This ISAE is effective for service auditor's assurance reports covering periods beginning on or after [date].

Objectives

8. The objectives of the service auditor are to:
 - (a) Obtain reasonable assurance about whether, in all material respects, based on suitable criteria:
 - (i) Management's description of the system is fairly presented;
 - (ii) The controls are suitably designed;
 - (iii) When included in the scope of the engagement, the controls operated effectively.
 - (b) Report in accordance with the service auditor's findings.

Definitions

9. For purposes of this ISAE, the following terms have the meanings attributed below:
 - (a) Carve-out method – Method of dealing with the services provided by a subservice organization, whereby the service organization's description of its system includes the nature of the activities performed by a subservice organization, but that subservice organization's relevant control objectives and related controls are excluded from the service organization's description of the system and from the scope of the service auditor's engagement. The service organization's description of the system and the scope of the service auditor's engagement include controls at the service organization to monitor the effectiveness of controls at the subservice organization, which may include the service organization's review of an assurance report on controls at the subservice organization.
 - (b) Complementary user entity controls – Controls that the service organization assumes, in the design of its service, will be implemented by user entities, and which, if necessary to achieve control objectives, are identified in the description of the system.
 - (c) Control objectives – The aim or purpose of a particular aspect of controls at the service organization. Control objectives ordinarily relate to risks that controls seek to mitigate.
 - (d) Controls at the service organization – The process designed, implemented and maintained by the service organization to provide reasonable assurance about the achievement of the control objectives that are relevant to the services covered by the

⁴ ISAE 3000, paragraphs 4 and 6.

service auditor's assurance report and that are likely to be relevant to user entities' internal control as it relates to financial reporting. (Ref: Para. A1)

- (e) Controls at a subservice organization – The process designed, implemented and maintained by a subservice organization to provide reasonable assurance about the achievement of the control objectives that are relevant to the services covered by the service auditor's assurance report.
- (f) Criteria – Benchmarks used to evaluate or measure a subject matter including, where relevant, benchmarks for presentation and disclosure. Suitable criteria are required for reasonably consistent evaluation or measurement of a subject matter within the context of professional judgment. Criteria need to be available to the intended users to allow them to understand how the subject matter has been evaluated or measured. See paragraphs 15-17 for minimum elements encompassed by criteria that are suitable for engagements to report on controls at the service organization.
- (g) Inclusive method – Method of dealing with the services provided by a subservice organization, whereby the service organization's description of its system includes the nature of the services performed by a subservice organization, and that subservice organization's relevant control objectives and related controls are included in the service organization's description of the system and in the scope of the service auditor's engagement.
- (h) Internal audit function – The service organization's internal auditors and others (for example, a compliance or risk department) who perform similar activities to internal auditors.
- (i) Report on the description and design of controls at a service organization (referred to in this ISAE as a "Type A report") – A report that comprises:
 - (i) A description of the service organization's system prepared by management of the service organization;
 - (ii) A written assertion by the service organization's management that, in all material respects, and based on suitable criteria:
 - a. The description fairly presents the service organization's system that had been designed and implemented as at the specified date;
 - b. The controls related to the control objectives stated in the description were suitably designed as at the specified date; and
 - (iii) A service auditor's assurance report that conveys reasonable assurance about the matters in (ii)a.-b. above.
- (j) Report on the description, design and operating effectiveness of controls at a service organization (referred to in this ISAE as a "Type B report") – A report that comprises:
 - (i) A description of the service organization's system prepared by management of the service organization;

- (ii) A written assertion by the service organization’s management that, in all material respects, and based on suitable criteria:
 - a. The description fairly presents the service organization’s system that had been designed and implemented throughout the specified period;
 - b. The controls related to the control objectives stated in the description were suitably designed throughout the specified period; and
 - c. The controls related to the control objectives stated in the description operated effectively throughout the specified period;
- (iii) A service auditor’s assurance report that:
 - a. Conveys reasonable assurance about the matters in (ii)a.-c. above; and
 - b. Includes a description of the service auditor’s tests of controls and the results thereof.
- (k) Service auditor – An auditor who provides an assurance report on the controls of a service organization.
- (l) Service organization – A third party organization (or segment of a third party organization) that provides services to user entities that are part of those entities’ information system relevant to financial reporting.
- (m) Service organization’s system –The policies and procedures designed, implemented and maintained by the service organization to provide user entities with the services covered by the service auditor’s assurance report. The description of the system prepared by management of the service organization includes identification the services covered, the period to which the description relates, control objectives and related controls.
- (n) Subservice organization – A service organization used by another service organization to perform some of the services provided to user entities that are part of those user entities’ information systems relevant to financial reporting.
- (o) Test of controls – A procedure designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, errors that could result in the non-achievement of specified control objectives.
- (p) User auditor – An auditor who audits and reports on the financial statements of a user entity.
- (q) User entity – An entity that uses a service organization.

Requirements

ISAE 3000

10. In addition to this ISAE, the service auditor shall comply with ISAE 3000.

Ethical Requirements

11. The service auditor shall comply with relevant ethical requirements, including those pertaining to independence, relating to assurance engagements. (Ref: Para. A2)

Unless the service auditor is required by law or regulation to accept or continue an engagement to report on controls at a service organization,

12. ~~F~~ the service auditor shall continue (or accept where applicable) an engagement only if: (Ref: Para. A3)
- (a) The service auditor's (preliminary) knowledge of the engagement circumstances indicates that:
 - (i) The criteria to be used will be suitable and available to the intended users;
 - (ii) The service auditor will have access to sufficient appropriate evidence to the extent necessary; and
 - (iii) The description of the system included in the scope of the engagement will not be so limited that it is unlikely that the engagement has a rational purpose.
 - (b) In agreeing the terms of the engagement, management of the service organization acknowledges and understands its responsibility for:
 - (i) Preparing and presenting the description of the system and accompanying assertion, including the completeness, accuracy and method of presentation of the description and assertion;
 - (ii) Stating in the assertion the criteria used;
 - (iii) Stating the control objectives (where not specified by law or regulation, or another party, for example a user group or a professional body), and identifying the risks that threaten their achievement;
 - (iv) Designing, implementing and maintaining controls to provide reasonable assurance that the stated control objectives will be achieved; and
 - (v) Providing the service auditor with:
 - a. All information, such as records and documentation, and other matters that are relevant to the preparation and presentation of the description of the system and accompanying assertion;
 - b. Any additional information that the service auditor may request; and
 - c. Unrestricted access to those within the service organization from whom the service auditor determines it necessary to obtain evidence.
13. If management requests a change in the scope of the engagement before the completion of the engagement, the auditor shall be satisfied that there is a reasonable justification for the change. (Ref: Para. A4)

Assessing the Suitability of the Criteria

14. As required by ISAE 3000, the service auditor shall assess whether the service organization has used suitable criteria in preparing and presenting the description of the system, in evaluating whether controls are suitably designed, and, in the case of a Type B report, in evaluating whether controls are operating effectively.⁵

In applying suitable

the auditor shall determine,

15. ~~Suitable~~ criteria for evaluating whether the description of the system is fairly presented, ~~shall encompass~~ at a minimum whether the description:

- (a) Presents how the service organization's system made available to user entities has been designed and implemented to process relevant transactions, including, as appropriate:
 - (i) The classes of transactions processed;
 - (ii) The procedures, within both information technology and manual systems, by which transactions are initiated, recorded, processed, corrected as necessary, and transferred to the reports presented to user entities;
 - (iii) The related accounting records, supporting information and specific accounts that are used to initiate, record, process and report transactions; this includes the correction of incorrect information and how information is transferred to the reports presented to user entities;
 - (iv) How the service organization's system captures significant events and conditions, other than transactions;
 - (v) The process used to prepare reports presented to user entities;
 - (vi) The stated control objectives and controls designed to achieve those objectives; and
 - (vii) Other aspects of the service organization's control environment, risk assessment process, information system (including the related business processes) and communication, control activities and monitoring controls that are relevant to the services provided.
- (b) Does not omit or distort information relevant to the scope of the service organization's system being described, while acknowledging that the description is presented to meet the common needs of a broad range of user entities and their auditors and may not, therefore, include every aspect of the service organization's system that each individual user entity and its auditor may consider important in its particular environment.

In applying suitable

16. ~~Suitable~~ criteria for evaluating whether controls are suitably designed to provide reasonable assurance that the stated control objectives will be achieved, ~~shall encompass~~ at a minimum whether:

- (a) The risks that threaten achievement of the control objectives stated in the description have been identified; and

Criteria are the standards or benchmarks used to measure and present the subject matter and against which the practitioner evaluates the subject matter. In assessing the suitability of criteria, the auditor shall determine if the criteria include each of the following attributes:

- a. *Objectivity* -- freedom from bias.
- b. *Measurability* -- permitting reasonably consistent qualitative or quantitative measurements of the subject matter.
- c. *Completeness* -- sufficiently complete so that those relevant factors that would alter a conclusion about subject matter are not omitted.
- d. *Relevance* -- having a significant relationship to the subject matter.

- (b) The identified controls would, if operated as described, provide reasonable assurance that those risks do not prevent the stated control objectives from being achieved.
17. Suitable criteria for evaluating whether controls have operated effectively to provide reasonable assurance that the stated control objectives identified in the description will be achieved shall encompass at a minimum whether the controls were consistently applied as designed. This includes whether manual controls were applied by individuals who have the appropriate competence and authority. (Ref: Para. A5)

Materiality

18. The service auditor shall consider materiality with respect to the fair presentation of the description, the suitability of the design of controls and, in the case of a Type B report, the operating effectiveness of controls when planning and performing the engagement. (Ref: Para. A6)

Using the Work of an Internal Audit Function

Obtaining an Understanding of the Internal Audit Function

19. The service auditor shall obtain an understanding of the aspects of the internal audit function that are relevant to the engagement. (Ref: Para. A7-A8)

Planning to Use the Work of the Internal Audit Function

20. When the service auditor intends to use the work of the internal audit function, the service auditor shall evaluate:
- (a) The objectivity and technical competence of members of the internal audit function;
 - (b) Whether the internal audit function is carried out with due professional care; and
 - (c) The effect of any constraints or restrictions placed on the internal audit function by management or those charged with governance.
21. In making judgments about the effect of the internal audit function's work on the service auditor's procedures, the service auditor shall consider:
- (a) The significance of that work to the service auditor's conclusions; and
 - (b) The degree of subjectivity involved in the evaluation of the evidence gathered in support of those conclusions.

Using the Work of the Internal Audit Function

22. When the service auditor uses specific work of the internal audit function, the service auditor shall perform procedures to evaluate the adequacy of that work.
23. When evaluating specific work performed by the internal audit function, the service auditor shall consider the adequacy of the scope of work and whether the evaluation of the internal audit function remains appropriate. The service auditor shall evaluate whether:
- (a) The work is performed by persons having appropriate skills and expertise;

- (b) The work is properly supervised, reviewed and documented;
- (c) Sufficient appropriate evidence is obtained to be able to draw reasonable conclusions;
- (d) Conclusions reached are appropriate in the circumstances and any reports prepared are consistent with the results of the work performed; and
- (e) Any exceptions or unusual matters disclosed by the internal audit function are properly resolved.

Effect on the Service Auditor's Assurance Report

- 24. If the work of the internal audit function has been used, the service auditor shall make no reference to that work in the section of the service auditor's assurance report that contains the service auditor's opinion. Notwithstanding its degree of autonomy and objectivity, the internal audit function is not independent of the service organization. The service auditor has sole responsibility for the opinion expressed in the service auditor's assurance report and, accordingly, that responsibility is not reduced by the service auditor's use of the work of the internal audit function.
- 25. In the case of a Type B report, if the work of the internal audit function has been used in performing tests of controls, that part of the service auditor's assurance report that describes the service auditor's tests of controls and the results thereof shall include a description of the internal auditor's work and of the service auditor's procedures with respect to that work.

Using the Work of a Service Auditor's Expert

The Capabilities, Competence and Objectivity of the Service Auditor's Expert

- 26. When the service auditor intends to use the work of a service auditor's expert, the service auditor shall evaluate whether the service auditor's expert whose work is to be used has the necessary capabilities, competence and objectivity for the purposes of the engagement. In the case of a service auditor's external expert, the evaluation of objectivity shall include inquiry regarding interests and relationships that may create a threat to that expert's objectivity.

Obtaining an Understanding of the Field of Expertise of the Service Auditor's Expert

- 27. The service auditor shall obtain a sufficient understanding of the field of expertise of the service auditor's expert to enable the service auditor to:
 - (a) Determine the nature, scope and objectives of that expert's work for the purposes of the engagement; and
 - (b) Evaluate the adequacy of that work for the purposes of the engagement.

Agreement with the Service Auditor's Expert

- 28. The service auditor shall agree, in writing when appropriate, the following matters with the service auditor's expert:
 - (a) The nature, scope and objectives of that expert's work;
 - (b) The respective roles of the service auditor and that expert; and

- (c) The nature, timing and extent of communication between the service auditor and that expert, including the form of any report to be provided by that expert.

Evaluating the Adequacy of the Service Auditor’s Expert’s Work

- 29. The service auditor shall evaluate the adequacy of the service auditor’s expert’s work for the purposes of the engagement.

Effect on the Service Auditor’s Assurance Report

- 30. If the work of a service auditor’s expert has been used, the service auditor shall make no reference to that work in the section of the service auditor’s assurance report that contains the service auditor’s opinion. The service auditor has sole responsibility for the opinion expressed in the service auditor’s assurance report and, accordingly, that responsibility is not reduced by the service auditor’s use of the work of a service auditor’s expert.
- 31. In the case of a Type B report, if the work of a service auditor’s external expert has been used in performing tests of controls, that section of the service auditor’s assurance report that describes the service auditor’s tests of controls and the results thereof shall include a description of the service auditor’s external expert’s work and of the service auditor’s procedures with respect to that work.

Obtaining an Understanding of the Service Organization’s System

- 32. The service auditor shall obtain an understanding of the service organization’s system, including controls, that are included in the scope of the engagement. (Ref: Para. A9-A10)

Obtaining Evidence Regarding the Description

- 33. The service auditor shall obtain and read the service organization’s description of the system, and shall evaluate whether those aspects of the description included in the scope of the engagement are presented fairly, including whether: (Ref: Para. A11-A12)
 - (a) Stated control objectives are reasonable in the circumstances; (Ref: Para. A13)
 - (b) Controls identified in the description were implemented;
 - (c) Complementary user entity controls, if any, are adequately described; and
 - (d) Services performed by a subservice organization, if any, are adequately described, including whether the inclusive method or the carve-out method has been used in relation to them. (Ref: Para. A14)
- 34. The service auditor shall confirm the implementation of the service organization’s system through other procedures in combination with inquiries of management and other service organization personnel. Those other procedures shall include observation, and inspection of records and other documentation, of the manner in which transactions are processed through the system and controls are applied.

The service auditor shall perform the following procedures to obtain information for use in identifying controls and the related risks that the description of the system is not fairly stated or that stated control objectives will not be achieved due to intentional acts by service organization personnel:

- a. Discuss, among the members of the service auditor’s team, factors at the service organization that could affect the risks that the description of the system is not fairly stated or the stated control objectives were not achieved due to intentional acts by service organization personnel, such as management override of the controls. (Ref: Para. A10c)
- b. Make inquiries of management and others within the service organization to obtain their views about such risks and how they are addressed.
- c. Consider whether factors exist at the service organization that increase such risks.
- d. Consider other information that comes to the service auditor’s attention that may be helpful in the identification of such risks.

The service auditor shall also (a) determine whether management’s risk assessment process addresses such risks, (b) evaluate the design of relevant controls and procedures at the service organization intended to address the identified risks, and (c) in the case of a Type B report, test the operating effectiveness of those controls. (Ref: Para. A10a-A10d)

Obtaining Evidence Regarding Design of Controls

35. The service auditor shall determine which of the controls at the service organization are necessary to achieve the stated control objectives included in the scope of the engagement, and shall assess whether those controls were suitably designed. This shall include: (Ref: Para. A15-A17)
- (a) Identifying the risks that threaten the achievement of the stated control objectives included in the scope of the engagement; and
 - (b) Evaluating the linkage of controls identified in the description with those risks.

Obtaining Evidence Regarding Effectiveness of Controls

36. If providing a Type B report, the service auditor shall test those controls that the service auditor has determined are necessary to achieve the stated control objectives included in the scope of the engagement, and assess their operating effectiveness throughout the period. (Ref: Para. A18-A22)
37. When designing and performing tests of controls, the service auditor shall:
- (a) Perform other procedures in combination with inquiry to obtain evidence about:
 - (i) How the control was applied;
 - (ii) The consistency with which the control was applied; and
 - (iii) By who or by what means the control was applied;
 - (b) Determine whether controls to be tested depend upon other controls (indirect controls), and if so, whether it is necessary to obtain evidence supporting the operating effectiveness of those indirect controls; and
 - (c) Determine means of selecting items for testing that are effective in meeting the objectives of the procedure. (Ref: Para. A23-A24) and whether sampling is appropriate,
38. When determining the extent of tests of controls, the service auditor shall consider the characteristics of the population to be tested, including the nature of controls, the frequency of their application (for example, monthly, daily, a number of times per day), and the expected rate of deviation. If the service auditor determines that sampling is appropriate, the service auditor may refer to ISA 530, *Audit Sampling and Other Means of Testing*, for guidance.

Attribute Sampling

39. When the service auditor uses attribute sampling, the service auditor shall: (Ref: Para. A23-A24)
- (a) Determine a sample size sufficient to conclude with an appropriately low level of sampling risk that the total rate of deviation does not exceed the tolerable rate of deviation;
 - (b) Select items for the sample in such a way that all sampling units in the population have a chance of selection;
 - (c) If a designed procedure is not applicable to a selected item, perform the procedure on a replacement item; and

- (d) If unable to apply the designed procedures, or suitable alternative procedures, to a selected item, treat that item as a deviation.

Nature and Cause of Deviations

- 40. The service auditor shall investigate the nature and cause of any deviations identified and shall determine whether:
 - (a) Identified deviations are within the expected rate of deviation and are acceptable; therefore, the testing that has been performed provides an appropriate basis for concluding that the control is operating effectively throughout the specified period;
 - (b) Additional testing of the control or of compensating controls is necessary to reach a conclusion on whether the controls relative to the stated control objective are operating effectively throughout the specified period; or
 - (c) The testing that has been performed provides an appropriate basis for concluding that the control did not operate effectively throughout the specified period.
- 41. In the extremely rare circumstances when the service auditor considers a deviation discovered in a sample to be an anomaly and no compensating controls have been identified, the service auditor shall obtain a high degree of certainty that such deviation is not representative of the population. The service auditor shall obtain this degree of certainty by performing additional procedures to obtain sufficient appropriate evidence that such deviations do not exist in the remainder of the population.

Written Representations

- 42. The service auditor shall request management or those charged with governance to provide written representations based on their knowledge and belief, having made appropriate inquiries for them to be able to provide such representations: (Ref: Para. A25-A26)
 - (a) That reaffirm the assertion accompanying the description of the system;
 - (b) Whether all records, documentation, unusual matters of which they are aware, and other information relevant to the assurance engagement have been made available to the service auditor; and
 - (c) That they have disclosed to the service auditor any of the following of which they are aware:
 - (i) Non-compliance with laws and regulations, or uncorrected errors attributable to the service organization's management or employees that may affect one or more user entities;
 - (ii) Design deficiencies in controls, including those for which management believes the cost of corrective action may exceed the benefits;
 - (iii) Instances where controls have not operated as described; and
 - (iv) Subsequent events regarding the services covered by the engagement that could have a significant effect on user entities.

43. These written representations shall be in the form of a representation letter addressed to the service auditor, and shall be as of the same date as the service auditor's assurance report.
44. If management does not provide one or more of the written representations requested by the service auditor, the auditor shall:
 - (a) Discuss the matter with management;
 - (b) Reconsider the assessment of the integrity of management; and
 - (c) Take appropriate actions, including determining the possible effect on the opinion in the service auditor's assurance report.

Other Information

45. The service auditor shall read the other information, if any, included in a document containing the description of the system and the service auditor's assurance report, to identify material inconsistencies, if any, with that description. While reading the other information for the purpose of identifying material inconsistencies, the service auditor may become aware of an apparent misstatement of fact in that other information.
46. If the service auditor becomes aware of a material inconsistency or an apparent misstatement of fact in the other information, the service auditor shall discuss the matter with management. If the service auditor concludes that there is a material inconsistency or a misstatement of fact in the other information that management refuses to correct, the service auditor shall take further appropriate action.

Subsequent Events

47. The service auditor shall inquire whether management is aware of any events subsequent to the period covered by the description of the system up to the date of the service auditor's assurance report that could have a significant effect on the service auditor's assurance report. If the service auditor is aware of a subsequent event that could have a significant effect on the service auditor's assurance report, and information about that event is not disclosed by the service organization, the service auditor shall disclose it in the service auditor's assurance report.
48. The service auditor has no obligation to perform any procedures regarding the description of the system, or the suitability of design or operating effectiveness of controls after the date of the service auditor's assurance report.

Documentation

49. The service auditor shall prepare documentation so as to enable an experienced service auditor, having no previous connection with the engagement, to understand:
 - (a) The nature, timing, and extent of the procedures performed to comply with this ISAE and applicable legal and regulatory requirements;
 - (b) The results of the procedures and the evidence obtained; and

- (c) Significant matters arising during the engagement, and the conclusions reached thereon and significant professional judgments made in reaching those conclusions.
50. In documenting the nature, timing and extent of procedures performed, the service auditor shall record:
 - (a) The identifying characteristics of the specific items or matters being tested;
 - (b) Who performed the procedures and the date such procedures were completed; and
 - (c) Who reviewed the work performed and the date and extent of such review.
 51. The service auditor shall document discussions of significant matters with the service organization and others including when and with whom the discussions took place.
 52. If the service auditor has identified information that is inconsistent with the service auditor's final conclusion regarding a significant matter, the service auditor shall document how the service auditor addressed the inconsistency in forming the final conclusion.
 53. The service auditor shall complete the assembly of the final engagement file on a timely basis after the date of the service auditor's assurance report.
 54. After the assembly of the final engagement file has been completed, the service auditor shall not delete or discard documentation before the end of its retention period.
 55. If the service auditor finds it necessary to modify existing engagement documentation or add new documentation after the assembly of the final engagement file has been completed, the service auditor shall, regardless of the nature of the modifications or additions, document:
 - (a) When and by whom they were made, and (where applicable) reviewed;
 - (b) The specific reasons for making them; and
 - (c) Their effect, if any, on the service auditor's conclusions.

Preparing the Service Auditor's Assurance Report

Content of the Service Auditor's Assurance Report

56. The service auditor's assurance report shall include the following basic elements: (Ref: Para. A27)
 - (a) A title that clearly indicates the report is an independent service auditor's assurance report.
 - (b) An addressee.
 - (c) Identification of:
 - (i) The description of the system, and management's assertion, which includes the matters described in paragraph 9(j)(ii) for a Type B report, or paragraph 9(i)(ii) for a Type A report.
 - (ii) If parts of the description of the system are not covered by the service auditor's opinion, an identification of those parts.

- (iii) If the description refers to the need for complementary user entity controls, a statement that the service auditor has not evaluated the suitability of design or operating effectiveness of complementary user entity controls, and that the stated control objectives can be achieved only if complementary user entity controls are suitably designed or operating effectively, along with the controls at the service organization.
 - (iv) If services are performed by a subservice organization, those services and whether the inclusive method or the carve-out method has been used in relation to them. Where the carve-out method has been used, a statement that the description of the system excludes the control objectives and related controls at relevant subservice organizations, and that the service auditor's procedures do not extend to the subservice organization. Where the inclusive method has been used, a statement that the description of the system includes the stated control objectives and related controls at the subservice organization, and that the service auditor's procedures included the subservice organization.
- (d) Identification of the criteria, and the party specifying the control objectives.
 - (e) A statement of the limitations of controls and, in the case of a Type B report, of the risk of projecting to future periods any evaluation of the effectiveness of controls.
 - (f) Identification of the purpose(s) and intended users of the service auditor's assurance report. (Ref: Para. A28)
 - (g) A description of the service organization's and the service auditor's responsibilities, including a statement that the service organization is responsible for:
 - (i) Preparing and presenting the description of the system, and accompanying assertion, including the completeness, accuracy and method of presentation of the description and assertion;
 - (ii) Providing the services covered by the description of the system;
 - (iii) Stating the control objectives (where not identified by law or regulation, or another party, for example a user group or a professional body), and the risks that threaten their achievement; and
 - (iv) Designing, implementing and maintaining controls to achieve the stated control objectives.
 - (h) A statement that the engagement was performed in accordance with ISAE 3402, "Assurance Reports on Controls at a Third Party Service Organization."
 - (i) A summary of the service auditor's procedures to obtain reasonable assurance and, in the case of a Type A report, a statement that the service auditor has not performed any procedures regarding the operating effectiveness of controls and therefore no opinion is expressed thereon.
 - (j) The service auditor's opinion, expressed in the positive form, on whether, in all material respects, based on suitable criteria:

- (i) In the case of a Type B report:
 - a. The description fairly presents the service organization’s system that had been designed and implemented throughout the specified period;
 - b. The controls related to the control objectives stated in the description were suitably designed throughout the specified period; and
 - c. The controls the service auditor tested operated effectively throughout the specified period.
 - (ii) In the case of a Type A report:
 - a. The description fairly presents the service organization’s system that had been designed and implemented as at the specified date; and
 - b. The controls related to the control objectives stated in the description were suitably designed as at the specified date.
 - (k) The date of the service auditor’s assurance report.
 - (l) The name of the service auditor, and the city where the service auditor maintains the office that has responsibility for the engagement.
57. In the case of a Type B report, the service auditor’s assurance report shall include a separate section after the opinion, or an attachment, that describes the service auditor’s tests of controls and the results thereof. In describing the tests of controls, the auditor shall clearly state which controls have been tested and the period during which they were tested, identify whether the items tested represent all or a selection of the items in the population, and indicate the nature of the tests in sufficient detail to enable user auditors to determine the effect of such tests on their risk assessments. If deviations have been identified, the service auditor shall include the extent of testing performed by the service auditor that led to identification of the deviations, and the number of deviations noted. The service auditor shall report deviations even if, on the basis of tests performed, the service auditor has concluded that the related control objective has been achieved. (Ref: Para. A29)

Modified Opinions

58. If the service auditor concludes that: (Ref: Para. A30)
- (a) management’s description of the system is not presented fairly in all material respects;
 - (b) the controls are not suitably designed to provide reasonable assurance that the stated control objectives will be achieved if the controls operate effectively;
 - (c) in the case of a Type B report, the controls did not operate effectively throughout the specified period; or
 - (d) the service auditor is unable to obtain sufficient appropriate evidence,
- the service auditor’s opinion shall be modified, and the service auditor’s assurance report shall contain a clear description of all the reasons for the modification.

Other Communication Responsibilities

59. If the service auditor becomes aware of non-compliance with laws and regulations, or uncorrected errors attributable to the service organization that are not clearly trivial and may affect one or more user entities, the service auditor shall determine whether this information has been communicated appropriately to affected user entities. If the information has not been so communicated and management of the service organization is unwilling to do so, the service auditor shall take appropriate action. (Ref: Para. A31)

Application and Other Explanatory Material

Definitions (Ref: Para. 9(d))

- A1. The process referred to in the definition of “controls at the service organization” at paragraph 9(d) invariably includes aspects of user entities’ information systems maintained by the service organization, and may also include aspects of one or more of the other components of internal control. For example, it may include aspects of the service organization’s control environment, monitoring, and control activities where they relate to the services provided. It does not, however, include controls at a service organization that are not related to the achievement of the control objectives stated in the description of the system, for example controls related to the preparation of the service organization’s own financial statements.

Ethical Requirements (Ref: Para. 11)

- A2. The service auditor is subject to independence requirements of the Code. However, in performing an engagement in accordance with this ISAE, the Code does not require the service auditor to be independent from each user entity.

Acceptance and Continuance (Ref: Para. 12-13)

- A3. The requirements of paragraph 12 do not preclude a service auditor from using this ISAE where required by law or regulation to accept or continue an engagement, for example, in the public sector, if the service auditor’s assurance report is modified appropriately and clearly indicates the reason that would otherwise have caused the service auditor to decline the engagement.
- A4. A request to change the scope of the engagement may not have a reasonable justification when, for example, the request is made:
- To exclude certain aspects of controls at the service organization from the scope of the engagement because of the likelihood that the service auditor’s opinion would be modified with respect to those aspects.
 - To change the report from a Type B to a Type A because of the likelihood that the service auditor’s opinion would be modified with respect to the operating effectiveness of controls.

Assessing the Suitability of the Criteria (Ref: Para. 14-17)

A5. ISAE 3000 requires the service auditor, amongst other things, to assess the suitability of criteria, and the appropriateness of the subject matter.⁶ The subject matter is the underlying condition of interest to intended users of an assurance report. The following table identifies the subject matter and minimum criteria for each of the opinions in Type B and Type A reports.

	<i>Subject matter</i>	<i>Criteria</i>	<i>Comment</i>	
<i>Opinion about the fair presentation of the description of the system (Type A and Type B reports)</i>	The system that is relevant to services covered by the service auditor’s assurance report.	The description is fairly presented if it: (a) presents how the service organization’s system made available to user entities has been designed and implemented to process relevant transactions including the matters identified in paragraph 15(a); and (b) does not omit or distort information relevant to the scope of the service organization’s system being described, while acknowledging that the description is presented to meet the common needs of a broad range of user entities and may not, therefore, include every aspect of the service organization’s system that each individual user entity may consider important in its own particular environment.	The specific wording of the criteria for this opinion may need to be tailored to be consistent with criteria established by, for example, law or regulation, user groups, or a professional body. Examples of criteria for this opinion are provided in the illustrative assertion in Appendix 1. Paragraphs A11-A14 offer further guidance on determining whether these criteria are met. (In terms of the requirements of ISAE 3000, the subject matter information ⁷ for this opinion is the description of the system and the service organization’s assertion that the description is presented fairly.)	
<i>Opinion about suitability of design, and operating effectiveness (Type B reports)</i>	The design and operating effectiveness of those controls that are necessary to achieve the stated control objectives	The controls are suitably designed and operating effectively if: (a) the risks that threaten achievement of the control objectives stated in the description have been identified; (b) the identified controls would, if operated as described, provide reasonable assurance that those risks do not prevent the stated	When the criteria for this opinion are met, controls will have provided reasonable assurance that the related control objectives were achieved throughout the specified period. (In terms of the requirements of ISAE	The control objectives, which are stated in the description, are part of the criteria for these opinions. The stated control objectives will differ from engagement to engagement. If, as part of forming the opinion on the

⁶ ISAE 3000, paragraphs 18-19.

⁷ The “subject matter information” is the outcome of the evaluation or measurement of the subject matter that results from applying the criteria to the subject matter.

	<i>Subject matter</i>	<i>Criteria</i>	<i>Comment</i>	
	relevant to services covered by the service auditor's assurance report.	control objectives from being achieved; and (c) those controls necessary for achieving the relevant control objectives were consistently applied as designed. This includes whether manual controls were applied by individuals who have the appropriate competence and authority.	3000, the subject matter information for this opinion is the service organization's assertion that controls are suitably designed and that they are operating effectively.)	description, the auditor concludes the stated control objectives are not fairly presented then those control objectives would not be suitable as part of the criteria for forming an opinion on either the design or operating effectiveness of controls.
<i>Opinion about suitability of design (Type A reports)</i>	The suitability of the design of those controls that are necessary to achieve the stated control objectives relevant to services covered by the service auditor's assurance report.	The controls are suitably designed if: (a) the risks that threaten achievement of the control objectives stated in the description have been identified; and (b) the identified controls would, if operated as described, provide reasonable assurance that those risks do not prevent the stated control objectives from being achieved.	Meeting this criterion does not, of itself, provide any assurance that the related control objectives were achieved because no assurance has been obtained about the operation of controls. (In terms of the requirements of ISAE 3000, the subject matter information for this opinion is the service organization's assertion that controls are suitably designed.)	

Materiality (Ref: Para. 18)

A6. In an engagement to report on controls at a service organization, the concept of materiality relates to the information being reported on, not the financial statements of user entities. The service auditor plans and performs procedures to determine whether the service organization's description of the system is fairly stated in all material respects, whether controls at the service organization are suitably designed in all material respects and, in the case of a Type B report, whether controls at the service organization are operating effectively in all material respects. In applying the concept of materiality, the service auditor considers that the service auditor's assurance report provides information about the service organization's system to meet the common information needs of a broad range of user entities and their auditors who have an understanding of the manner in which the system is being used in a particular user entity for financial reporting by that user entity. Materiality with respect to the fair presentation of the description, and with respect to the design of controls, includes primarily the consideration of qualitative factors, for example, whether the description includes the significant aspects of

processing significant transactions, whether the description omits or distorts relevant information, and the ability of controls, as designed, to provide reasonable assurance that the stated control objectives would be achieved. Materiality with respect to the operating effectiveness of controls includes the consideration of both quantitative and qualitative factors, for example, the tolerable rate and observed rate of deviation (a quantitative matter), and the nature and cause of any observed deviation (a qualitative matter).

Using the Work of an Internal Audit Function

Obtaining an Understanding of the Internal Audit Function (Ref: Para. 19)

- A7. An internal audit function may be responsible for providing analyses, evaluations, assurances, recommendations, and other information to management and those charged with governance. An internal audit function at a service organization may perform activities related to the service organization's internal control, or activities related to the services and systems, including controls, that the service organization is providing to user entities.
- A8. The scope and objectives of an internal audit function vary widely and depend on the size and structure of the service organization and the requirements of management and those charged with governance. Internal audit function activities may include one or more of the following:
- Monitoring of the service organization's internal control or the application processing systems, including controls, provided to user entities. The internal audit function may be assigned specific responsibility for reviewing controls, monitoring their operation and recommending improvements thereto.
 - Examination of financial and operating information. The internal audit function may be assigned to review the means used to identify, measure, classify and report financial and operating information, and specific inquiry and other procedures into individual items including detailed testing of transactions, balances and procedures.
 - Evaluation of the economy, efficiency and effectiveness of operating activities including non-financial activities of a service organization.
 - Evaluation of compliance with laws, regulations and other external requirements, and with management policies and directives and other internal requirements.

Obtaining an Understanding of the Service Organization's System (Ref: Para. 32)

- A9. Obtaining an understanding of the service organization's system, including controls, included in the scope of the engagement, assists the service auditor in:
- Identifying the boundaries of the system, and how it interfaces with other systems.
 - Assessing whether the service organization's description fairly presents the system that has been designed and implemented.
 - Determining which controls are necessary to achieve the stated control objectives included in the scope of the engagement, and whether controls were suitably designed, and, in the case of a Type B report, operating effectively.

A10a. The procedures and controls the service organization implements to address the risks that the description of the system is not fairly presented or that the control objectives were not achieved due to intentional acts by service organization personnel may include relevant aspects of the control environment, monitoring, the information system used to process user transactions, and control activities.

A10b. In addition to management override of controls at the service organization, other intentional acts by service organization personnel that may affect the fairness of the presentation of the description of the system or the completeness or achievement of the stated control objectives include:

- Misappropriation of user entity assets by service organization personnel.
- Creation, by service organization personnel, of false or misleading documents or records of user organization transactions processed by the service organization.

A10. Procedures to obtain this understanding may include:

- Inquiring of management and of others within the service organization who, in the service auditor's judgment, may have relevant information.
- Observing operations and inspecting documents, reports, printed and electronic records of transaction processing.
- Inspecting a selection of agreements between the service organization and user entities to identify their common terms.

Obtaining Evidence Regarding the Description (Ref: Para. 33)

A11. Considering the following questions may assist the service auditor in determining whether those aspects of the description included in the scope of the engagement are fairly stated in all material respects:

- Does the description address the major aspects of the service provided (within the scope of the engagement) that could reasonably be expected to be relevant to the common needs of a broad range of user auditors in planning their audits of user entities' financial statements?
- Is the description presented at a level of detail that could reasonably be expected to provide a broad range of user auditors with sufficient information to obtain an understanding of internal control in accordance with ISA 315 (Redrafted)?⁸ The description need not address every aspect of the service organization's processing or the services provided to user entities, and need not be so detailed as to potentially allow a reader to compromise security or other controls at the service organization.
- Is the description prepared and presented in a manner that does not omit or distort information that may affect the common needs of a broad range of user auditors' decisions, for example, does the description contain any significant omissions or inaccuracies in processing of which the service auditor is aware?
- Have the controls identified in the description actually been implemented?
- Are complementary user entity controls, if any, adequately described? In most cases, the description of control objectives is worded such that the control objectives are capable of being achieved through effective operation of controls implemented by the service organization alone. In some cases, however, the control objectives stated in the description cannot be achieved by the service organization alone because their achievement requires particular controls to be implemented by user entities. This may be the case where, for example, the control objectives are specified by a regulatory authority. When the description does include complementary user entity controls, the description separately identifies those controls.

⁸ ISA 315 (Redrafted), "Identifying and Assessing Risks of Material Misstatement Through Understanding the Entity and Its Environment."

A10c. Factors that may increase the risk of management override include unrealistic processing schedules, significant increases in processing volumes that exceed normal processing capacity, or an environment in which established procedures and controls are not consistently followed. Depending on the nature of the services provided by the service organization and the extent to which the service organization initiates, records, processes, records and reports transactions for user entities, a significant risk of misappropriation of user entity assets by service organization personnel may exist. Factors that may increase the risk of misappropriation of assets include inadequate supervision or monitoring, processing or maintaining records for large amounts of cash or investments, inadequate segregation of duties or independent checks, and inadequate physical or electronic safeguards over cash or investments. The risk of override and the risk of misappropriation of user entity assets may result in false or misleading records or documents being provided to user organizations. The service auditor's procedures are affected by the extent to which management has identified and addressed the identified risks thorough monitoring or other controls, and the nature and extent of the identified risks.

A10d. While ISA section 240, *The Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements*, is not applicable to engagements performed under this attestation standard, it nonetheless provides a framework that may be useful to the service auditor to identify and respond to risks that the description of the system is not fairly stated or that stated control objectives will not be achieved due to intentional actions by service organization personnel.

A12. The service auditor's procedures to evaluate the fair presentation of the description may include:

- Considering the nature of user entities and how the services provided by the service organization are likely to affect them, for example, the predominant type(s) of user entities, and whether user entities are regulated by government agencies.
- Reading standard contracts, or standard terms of contracts, (if applicable) with user entities to gain an understanding of the service organization's contractual obligations.
- Observing procedures performed by service organization personnel.
- Reviewing the service organization's policy and procedure manuals and other systems documentation, for example, flowcharts and narratives.

A13. Paragraph 33(a) requires the service auditor to evaluate whether the stated control objectives are reasonable in the circumstances. Considering the following questions may assist the service auditor in this evaluation:

- Have the stated control objectives been designated by the service organization or by outside parties such as regulatory authorities, a user group, a professional body or others?
- Where the stated control objectives have been specified by management, do they relate to the types of assertions commonly embodied in the broad range of user entities' financial statements to which controls at the service organization could reasonably be expected to relate? Although the service auditor ordinarily will not be able to determine how controls at a service organization specifically relate to the assertions embodied in individual user entities' financial statements, the service auditor's understanding of the nature of the service organization's system, including controls, and services being provided is used to identify the types of assertions to which those controls are likely to relate.
- Where the stated control objectives have been specified by management, are they complete? A complete set of control objectives can provide a broad range of user auditors with a framework to assess the effect of controls at the service organization on the assertions commonly embodied in user entities' financial statements.

A14. If the inclusive method has been used, it is important that the description adequately differentiates between controls at the service organization and controls at the subservice organization. If the carve-out method is used, it is important that the description identifies the functions that are performed by the subservice organization, but it need not describe the detailed processing or controls at the subservice organization.

Obtaining Evidence Regarding the Design of Controls (Ref: Para. 35)

A15. From the viewpoint of a *user auditor*, a control is suitably designed if individually or in combination with other controls, it would, when complied with satisfactorily, provide reasonable assurance that material misstatements, whether due to fraud or error, are prevented, or detected and corrected. A *service auditor*, however, is not aware of the

circumstances at individual user entities that would determine whether or not a misstatement resulting from a control deviation is material to those user entities. Therefore, from the viewpoint of a service auditor, a control is suitably designed if individually or in combination with other controls, it would, when complied with satisfactorily, provide reasonable assurance that stated control objectives are achieved.

- A16. A service auditor may consider using flowcharts, questionnaires, or decision tables to facilitate understanding the design of the controls.
- A17. Controls may consist of a number of integrated activities directed at the achievement of various control objectives. Consequently, where the service auditor evaluates certain activities as being ineffective in achieving a particular control objective, the existence of other activities, sometimes known as compensating controls, may nonetheless allow the service auditor to conclude that controls related to the stated control objective are suitably designed.

Obtaining Evidence Regarding the Effectiveness of Controls

Assessing Operating Effectiveness (Ref: Para. 36)

- A18. From the viewpoint of a *user auditor*, a control is operating effectively if individually or in combination with other controls, it provides reasonable assurance that material misstatements, whether due to fraud or error, are prevented, or detected and corrected. A *service auditor*, however, is not aware of the circumstances at individual user entities that would determine whether or not a misstatement resulting from a control deviation is material. Therefore, from the viewpoint of a service auditor, a control is operating effectively if individually or in combination with other controls, it provides reasonable assurance that stated control objectives are achieved. Similarly, a service auditor is not in a position to determine whether any observed control deviation would result in a material misstatement from the viewpoint of an individual user entity.
- A19. Obtaining an understanding of controls sufficient to opine on the suitability of their design is not sufficient evidence regarding their operating effectiveness, unless there is some automation that provides for the consistent operation of the controls as they were designed and implemented. For example, obtaining information about the implementation of a manual control at a point in time does not provide evidence about operation of the control at other times. However, because of the inherent consistency of IT processing, performing procedures to determine the design of an automated control and whether it has been implemented may serve as evidence of that control's operating effectiveness, depending on the service auditor's assessment and testing of other controls, such as those over program changes.
- A20. To be useful to user auditors, a Type B report ordinarily covers a minimum period of six months. If the period is less than six months, the service auditor may consider it appropriate to describe the reasons for the shorter period in the service auditor's assurance report. Circumstances that may result in a report covering a period of less than six months include when (a) the service auditor is engaged close to the date by which the report on controls is to be issued; (b) the service organization (or a particular system or application) has been in operation for less than six months; or (c) significant changes have been made to the controls

and it is not practicable either to wait six months before issuing a report or to issue a report covering the system both before and after the changes.

- A21. Certain control procedures may not leave evidence of their operation that can be tested at a later date and accordingly, the service auditor may find it appropriate to test the operating effectiveness of such control procedures at various times throughout the reporting period.
- A22. Evidence from prior engagements about the satisfactory operation of controls in prior periods cannot provide a basis for a reduction in testing, even if it is supplemented with evidence obtained during the current period. This is because the service auditor provides an opinion on the effectiveness of controls throughout each period, therefore sufficient evidence about the operation of controls during the current period is required for the service auditor to express that opinion.

Means of Selecting Items for Testing (Ref: Para. 37(c) and 39)

A23. The means of selecting items for testing available to the service auditor are:

- (a) Selecting all items (100% examination). This may be appropriate for testing controls that are applied infrequently, for example, quarterly, or when evidence regarding application of the control makes 100% examination efficient;
- (b) Selecting specific items. This may be appropriate where 100% examination would not be efficient and attribute sampling would not be effective, such as testing controls that enforce segregation of duties, or testing controls that are not applied sufficiently frequently to render a large population for attribute sampling, for example, controls that are applied monthly; and
- (c) Attribute sampling. This may be appropriate for testing controls that are applied frequently in a uniform manner and which leave documentary evidence of their application.

A24. While selective examination of specific items will often be an efficient means of obtaining evidence, it does not constitute attribute sampling. The results of procedures applied to items selected in this way cannot be projected to the entire population; accordingly, selective examination of specific items does not provide evidence concerning the remainder of the population. Attribute sampling, on the other hand, is designed to enable conclusions to be drawn about an entire population on the basis of testing a sample drawn from it.

Written Representations (Ref: Para. 42)

A25. The written representations reconfirming the service organization's assertion about the effective operation of controls may be based on ongoing monitoring activities, separate evaluations, or a combination of the two. Ongoing monitoring activities are often built into the normal recurring activities of a service organization and include regular management and supervisory activities. Internal auditors or personnel performing similar functions may contribute to the monitoring of a service organization's activities. Monitoring activities may also include using information from communications from external parties, such as customer

complaints and regulator comments, that may indicate problems or highlight areas in need of improvement.

A26. The written representations required by paragraph 42 are separate from, and in addition to, the assertion contained in the service organization's report on controls, as described in paragraph 9(j)(ii) for a Type B report, and paragraph 9(i)(ii) for a Type A report.

Preparing the Service Auditor's Assurance Report

Content of the Service Auditor's Assurance Report (Ref: Para.56)

A27. Illustrative examples of service auditors' assurance reports and related service organizations' management assertions are contained in Appendices 1 and 2.

Use of the Service Auditor's Assurance Report (Ref: Para. 56(f))

A28. ISAE 3000 requires that when the criteria used to evaluate or measure the subject matter are available only to specific intended users, or are relevant only to a specific purpose, the assurance report includes a statement restricting the use of the assurance report to those intended users or that purpose.⁹ The criteria used for engagements to report on controls at a service organization are relevant only for the purposes of providing information about the service organization's system, including controls, to those who have an understanding of how the system is used for financial reporting by user entities, and accordingly the service auditor's assurance report states that it is intended only for use by existing users and their financial statement auditors.

Description of the Service Auditor's Tests of Controls (Ref: Para. 57)

A29. In describing the nature of the service auditor's tests of controls for a Type B report, it assists readers if the service auditor's assurance report defines the types of tests performed. It also assists readers of the service auditor's assurance report if the service auditor includes:

- The results of all tests where deviations have been identified, even if compensating controls have been identified or the control tested has subsequently been removed from the description of the system.
- Information about causative factors for identified deviations, to the extent the service auditor has identified such factors.

Modified Opinions (Ref: Para. 58)

A30. Illustrative examples of elements of modified service auditor's assurance reports are contained in Appendix 3. ↑

Other Communication Responsibilities (Ref: Para. 59)

A31. Appropriate action when the service auditor becomes aware of non-compliance with laws and regulations, or uncorrected error that has not been communicated appropriately to

⁹ ISAE 3000, paragraph 49(f).

For further guidance on issuing a modified report, see ISAE 3000 paragraphs 51-53.

affected user entities, and management of the service organization is unwilling to do so, may include:

- Obtaining legal advice about the consequences of different courses of action.
- Communicating with those charged with governance of the service organization.
- Communicating with third parties (for example, a regulator) when required to do so.
- Modifying the service auditor's opinion, or adding an other matters paragraph.
- Withdrawing from the engagement.

Appendix 1

(Ref. Para. A27)

Example Management Assertions

The following example management assertions are for guidance only and are not intended to be exhaustive or applicable to all situations.

Example 1: Type B Assertion for Service Organization

Management's Assertion

We have prepared the accompanying description for existing customers of our *[the type or name of]* system and their auditors who have a sufficient understanding to consider it, along with other information including information about controls operated by customers themselves, when assessing the risks of material misstatements of customers' financial statements. We confirm that:

- (a) The accompanying description at pages *[bb-cc]* of the system fairly presents *[the type or name of]* system made available to existing customers for processing their transactions throughout the period *[date]* to *[date]*. The criteria we used in making this assertion were that the accompanying description:
 - (i) Presents how the system made available to existing customers has been designed and implemented to process relevant transactions, including:
 - The classes of transactions processed.
 - The procedures, within both information technology and manual systems, by which those transactions are initiated, recorded, processed, corrected as necessary, and transferred to the reports presented to existing customers.
 - The related accounting records, supporting information and specific accounts that are used to initiate, record, process and report transactions; this includes the correction of incorrect information and how information is transferred to the reports presented to existing customers.
 - How the system captures significant events and conditions, other than transactions.
 - The process used to prepare reports presented to existing customers.
 - The stated control objectives and controls designed to achieve those objectives.
 - Other aspects of our control environment, risk assessment process, information system (including the related business processes) and communication, control activities and monitoring controls that are relevant to processing and reporting existing customers' transactions.
 - (ii) Does not omit or distort information relevant to the scope of the system being described, while acknowledging that the description is presented to meet the common needs of a broad range of existing customers and their auditors and may not, therefore, include

every aspect of the system that each individual customer may consider important in its own particular environment.

- (b) The controls related to the control objectives stated in the accompanying description were suitably designed and operated effectively throughout the period *[date]* to *[date]*. The criteria we used in making this assertion were that:
- (i) The risks that threaten achievement of the control objectives stated in the description have been identified;
 - (ii) The identified controls would, if operated as described, provide reasonable assurance that those risks do not prevent the stated control objectives from being achieved; and
 - (iii) The controls were consistently applied as designed, including that manual controls were applied by individuals who have the appropriate competence and authority.

[Management (or Those Charged With Governance)]

Example 2: Type A Assertion for Service Organization

Management's Assertion

We have prepared the accompanying description for existing customers of our *[the type or name of]* system and their auditors who have a sufficient understanding to consider it, along with other information including information about controls operated by customers themselves, when obtaining an understanding of customers' information systems relevant to financial reporting. We confirm that:

- (a) The accompanying description at pages *[bb-cc]* of the system fairly presents *[the type or name of]* system made available to existing customers for processing their transactions as at *[date]*. The criteria we used in making this assertion were that the accompanying description:
- (i) Presents how the system made available to existing customers has been designed and implemented to process relevant transactions, including:
 - The classes of transactions processed.
 - The procedures, within both information technology and manual systems, by which those transactions are initiated, recorded, processed, corrected as necessary, and transferred to the reports presented to existing customers.
 - The related accounting records, supporting information and specific accounts that are used to initiate, record, process and report transactions; this includes the correction of incorrect information and how information is transferred to the reports presented to existing customers.
 - How the system captures significant events and conditions, other than transactions.
 - The process used to prepare reports presented to existing customers.
 - The stated control objectives and controls designed to achieve those objectives.

- Other aspects of our control environment, risk assessment process, information system (including the related business processes) and communication, control activities and monitoring controls that are relevant to processing and reporting existing customers' transactions.
- (ii) Does not omit or distort information relevant to the scope of the system being described, while acknowledging that the description is presented to meet the common needs of a broad range of existing customers and their auditors and may not, therefore, include every aspect of the system that each individual customer may consider important in its own particular environment.
- (b) The controls related to the control objectives stated in the accompanying description were suitably designed as at *[date]*. The criteria we used in making this assertion were that:
- (i) The risks that threaten achievement of the control objectives stated in the description have been identified; and
 - (ii) The identified controls would, if operated as described, provide reasonable assurance that those risks do not prevent the stated control objectives from being achieved.

[Management (or Those Charged With Governance)]

Appendix 2

(Ref. Para. A27)

Example Service Auditor’s Assurance Reports

The following examples of reports are for guidance only and are not intended to be exhaustive or applicable to all situations.

Example 1: Type B Service Auditor’s Assurance Report

**Independent Service Auditor’s Assurance Report on
the Description of Controls, their Design and Effective Operation**

To: XYZ Service Organization

Scope

We have been engaged to report on XYZ Service Organization’s description at pages [bb-cc] of [the type or name of] system made available to customers for processing their transactions throughout the period [date] to [date] (the description), and on the design and operation of controls related to the control objectives stated in the description.¹⁰

Management’s Responsibilities

Management of XYZ Service Organization is responsible for preparing and presenting the description and accompanying assertion at page [aa], including the completeness, accuracy and method of presentation of the description and assertion, providing the services covered by the description, stating the control objectives and identifying the risks that threaten their achievement, and designing, implementing and maintaining controls to achieve the stated control objectives.

Service Auditor’s Responsibilities

Our responsibility is to express an opinion on the description, and on the design and operation of controls related to the control objectives stated in that description, based on our procedures. We conducted our engagement in accordance with International Standard on Assurance Engagements 3402, “Assurance Reports on Controls at a Third Party Service Organization” issued by the International Auditing and Assurance Standards Board. That standard requires that we comply with ethical requirements, and plan and perform our procedures to obtain reasonable assurance whether, in all material respects, the description is fairly presented and the controls are suitably designed and operating effectively.

An assurance engagement on the description, design and effective operation of controls at a service organization involves performing procedures to obtain evidence about the disclosures in the description of the system, and the design and effective operation of controls. The procedures selected depend on the service auditor’s judgment, including the assessment of the risks that the description is not fairly presented, and that controls are not suitably designed or operating effectively, whether due

¹⁰ If some elements of the description are not included in the scope of the engagement, this is made clear in the assurance report.

to fraud or error. Our procedures included testing the operating effectiveness of those controls that we consider necessary to provide reasonable assurance that the control objectives stated in the description were achieved. An assurance engagement of this type also includes evaluating the overall presentation of the description, and the suitability of the objectives stated therein.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Limitations of Internal Controls at a Service Organization

Because of their nature, controls at a service organization may not prevent or detect all errors or omissions in processing or reporting transactions. Also, the projection of any evaluation of effectiveness to future periods is subject to the risk that controls at a service organization may become inadequate or fail.

Opinion

Our opinion has been formed on the basis of the matters outlined in this report. The criteria we used in forming our opinion were those described in management's assertion at page [aa]. In our opinion, in all material respects:

- (a) The description fairly presents the [the type or name of] system that had been designed and implemented throughout the period [date] to [date];
- (b) The controls related to the control objectives stated in the description were suitably designed throughout the period [date] to [date]; and
- (c) The controls we tested, which were those necessary to provide reasonable assurance that the control objectives stated in the description were achieved, operated effectively throughout the period [date] to [date].

Description of Tests of Controls

The specific controls that were tested and the nature, timing and results of those tests are listed on pages [yy-zz].

Intended Users and Purpose

This report and the description of tests of controls on pages [yy-zz] are intended only for existing customers of XYZ Service Organization's [type or name of] system, and their auditors, who have a sufficient understanding to consider it, along with other information including information about controls operated by customers themselves, when assessing the risks of material misstatements of customers' financial statements.

[Service auditor's signature]

[Date of the service auditor's assurance report]

[Service auditor's address]

Example 2: Type A Service Auditor’s Assurance Report**Independent Service Auditor’s Assurance Report on
the Description of Controls and their Design**

To: XYZ Service Organization

Scope

We have been engaged to report on XYZ Service Organization’s description at pages [bb-cc] of [the type or name of] system made available to customers for processing their transactions as at [date] (the description), and on the design of controls related to the control objectives stated in the description.¹¹

Management’s Responsibilities

Management of XYZ Service Organization is responsible for preparing and presenting the description and accompanying assertion at page [aa], including the completeness, accuracy and method of presentation of the description and the assertion, providing the services covered by the description, stating the control objectives and identifying the risks that threaten their achievement, and designing, implementing and maintaining controls to achieve the stated control objectives.

Service Auditor’s Responsibilities

Our responsibility is to express an opinion on the description, and on the design of controls related to the control objectives stated in that description, based on our procedures. We conducted our engagement in accordance with International Standard on Assurance Engagements 3402, “Assurance Reports on Controls at a Third Party Service Organization” issued by the International Auditing and Assurance Standards Board. That standard requires that we comply with ethical requirements, and plan and perform our procedures to obtain reasonable assurance whether, in all material respects, the description is fairly presented and the controls are suitably designed in all material respects.

An assurance engagement on the description and design of controls at a service organization involves performing procedures to obtain evidence about the disclosures in the description of the system, and the design of controls. The procedures selected depend on the service auditor’s judgment, including the assessment that the description is not fairly presented, and that controls are not suitable designed, whether due to fraud or error. An assurance engagement of this type also includes evaluating the overall presentation of the description, and the suitability of the objectives stated therein.

We did not perform any procedures regarding the operating effectiveness of controls included in the description, and accordingly do not express an opinion thereon.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

¹¹ If some elements of the description are not included in the scope of the engagement, this is made clear in the assurance report.

Limitations of Internal Controls at a Service Organization

Because of their nature, controls at a service organization may not prevent or detect all errors or omissions in processing or reporting transactions.

Opinion

Our opinion has been formed on the basis of the matters outlined in this report. The criteria we used in forming our opinion were those described in management's assertion at page [aa]. In our opinion, in all material respects:

- (a) The description fairly presents the [the type or name of] system that had been designed and implemented as at [date], and
- (b) The controls related to the control objectives stated in the description were suitably designed as at [date].

Intended Users and Purpose

This report is intended only for existing customers of XYZ Service Organization's [type or name of] system, and their auditors, who have a sufficient understanding to consider it, along with other information including information about controls operated by customers themselves, when obtaining an understanding of customers' information systems relevant to financial reporting.

[Service auditor's signature]

[Date of the service auditor's assurance report]

[Service auditor's address]

Appendix 3

(Ref. Para. A30)

Example Modified Service Auditor's Assurance Reports

The following examples of modified reports are for guidance only and are not intended to be exhaustive or applicable to all situations. They are based on the examples of reports in Appendix 2.

Example 1: Qualified opinion – management's description of the system is not presented fairly in all material respects

...

Service Auditor's Responsibilities

...

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

Basis for Qualified Opinion

The accompanying description states at page [mn] that XYZ Service Organization uses operator identification numbers and passwords to prevent unauthorized access to the system. Based on our procedures, which included inquiries of staff personnel and observation of activities, we have determined that operator identification numbers and passwords are employed in Applications A and B but not in Applications C and D.

Qualified Opinion

Our opinion has been formed on the basis of the matters outlined in this report. The criteria we used in forming our opinion were those described in management's assertion at page [aa]. In our opinion, except for the matter described in the Basis for Qualified Opinion paragraph:

(a) ...

Example 2: Qualified opinion – the controls are not suitably designed to provide reasonable assurance that the stated control objectives will be achieved if the controls operate effectively

...

Service Auditor's Responsibilities

...

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

Basis for Qualified Opinion

As discussed at page [mn] of the accompanying description, from time to time XYZ Service Organization makes changes in application programs to correct deficiencies or to enhance capabilities. The procedures followed in determining whether to make changes, in designing the changes and in implementing them, do not include review and approval by authorized individuals who are independent from those involved in making the changes. There are also no specified requirements to test such changes or provide test results to an authorized reviewer prior to implementing the changes.

Qualified Opinion

Our opinion has been formed on the basis of the matters outlined in this report. The criteria we used in forming our opinion were those described in management’s assertion at page [aa]. In our opinion, except for the matter described in the Basis for Qualified Opinion paragraph:

(a) ...

Example 3: Qualified opinion – the controls did not operate effectively throughout the specified period (Type B report only)

...

Service Auditor’s Responsibilities

...

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

Basis for Qualified Opinion

XYZ Service Organization states in its description that it has automated controls in place to reconcile loan payments received with the output generated. However, as noted at page [mn] of the description, this control was not operating effectively during the period from dd/mm/yyyy to dd/mm/yyyy due to a programming error. This resulted in the non-achievement of the control objective “Controls provide reasonable assurance that loan payments received are properly recorded” during the period from dd/mm/yyyy to dd/mm/yyyy. Management implemented a change to the program performing the calculation as of [date], and our tests indicate that it was operating effectively during the period from dd/mm/yyyy to dd/mm/yyyy.

Qualified Opinion

Our opinion has been formed on the basis of the matters outlined in this report. The criteria we used in forming our opinion were those described in management’s assertion at page [aa]. In our opinion, except for the matter described in the Basis for Qualified Opinion paragraph:

...

Example 4: Qualified opinion – the service auditor is unable to obtain sufficient appropriate evidence

...

Service Auditor's Responsibilities

...

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

Basis for Qualified Opinion

XYZ Service Organization states in its description that it has automated controls in place to reconcile loan payments received with the output generated. However, electronic records of the performance of this reconciliation for the period from *dd/mm/yyyy* to *dd/mm/yyyy* were deleted as a result of a computer processing error, and we were therefore unable to test the operation of this control for that period. Consequently, we were unable to determine whether the control objective "Controls provide reasonable assurance that loan payments received are properly recorded" operated effectively during the period from *dd/mm/yyyy* to *dd/mm/yyyy*.

Qualified Opinion

Our opinion has been formed on the basis of the matters outlined in this report. The criteria we used in forming our opinion were those described in management's assertion at page *[aa]*. In our opinion, except for the matter described in the Basis for Qualified Opinion paragraph:

(a) ...

PROPOSED CONFORMING AMENDMENT

Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services

Other International Standards

- 24a. Some International Standards identified in paragraphs 5-7 contain: objectives, requirements, application and other explanatory material, and introductory material and definitions. These terms are to be interpreted in a directly analogous way to how they are explained in the context of ISAs and financial statement audits in paragraphs 15-22.
- 24b. ~~The~~ Other International Standards identified in paragraphs 5-7 contain basic principles and essential procedures ...



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