



AUDIT &  
ASSURANCE  
FACULTY

## re:Assurance

Perspectives on assurance

ENGAGING  
POLICY MAKERS



# re:Assurance

An initiative from [the ICAEW Audit and Assurance Faculty](#)

All types of business, public and voluntary bodies, investors, governments, tax authorities, market regulators and their stakeholders need to be able to rely on credible information flows to make decisions. Confidence suffers when there is uncertainty about the integrity of information or its fitness for purpose.

The Institute of Chartered Accountants in England and Wales' (ICAEW) Audit and Assurance Faculty is a leading authority on external audit and other assurance services. It is recognised internationally by members, professional bodies and others as a source of expertise on issues related to audit and assurance.

Through the *re:Assurance* initiative, the ICAEW Audit and Assurance Faculty is promoting dialogue about external assurance: finding out where new assurance services could strengthen markets and enhance confidence by making information flows more credible; asking how the *International Framework for Assurance Engagements* can be applied and developed; and answering demands for practical guidance to meet emerging business needs.

*Perspectives on assurance* is a series of discussion papers within the *re:Assurance* initiative aimed at specific audiences; those with an interest in public policy, people in business and assurance practitioners. The aim of these papers is to stimulate dialogue.

*Perspectives on assurance: Engaging policy makers* explains the role of external assurance in society and considers public interest issues related to the provision and performance of assurance services.

*Perspectives on assurance: Engaging business* helps business and their stakeholders to understand the nature of external assurance, to identify business needs and expectations that could be met by external assurance and to solicit feedback based on practical experience.

*Perspectives on assurance: Engaging practitioners* aims to increase awareness amongst practitioners of the nature of external assurance and helps them to respond to opportunities for external assurance. It explains the key elements of the *International Framework for Assurance Engagements*, seeks feedback based on practical experience and identifies areas where there may be a need for new guidance.

Further information on the *re:Assurance* initiative, the current work programme and how to get involved is available at [www.icaew.com/assurance](http://www.icaew.com/assurance) or telephone Jo Iwasaki on + 44 (0)20 7920 8786.

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December 2007

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ISBN: 978-184152-530-3

Perspectives on assurance  
**Engaging policy makers**

# Perspectives on assurance

## Engaging policy makers

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## Share your views

This paper is written primarily for policy makers and others who have an interest in public policy. The Institute of Chartered Accountants in England and Wales' (ICAEW) Audit and Assurance Faculty is committed to exploring the role of external assurance in society and seeks to generate discussion of public interest issues relating to the provision and performance of external assurance services.

We want to discuss the issues identified in this discussion paper with policy makers and others who have an interest in external assurance and related public policy issues. Comments can be emailed to us but if you would like to talk to us please call the number below or send your contact details to our email address. Comments are requested by 30 June 2008.

In the discussion paper we pose a series of questions, which are reproduced below. We are particularly interested in views on these questions.

The discussion paper also explores a number of issues which might benefit from further research. We are keen to hear about any research which is being or could be conducted in these areas.

### External assurance and society

1. This discussion paper sets out a number of factors that might influence the need for external assurance, such as new technology, business practices, changing expectations of stakeholders and demands for further information and new regulations which raise concerns about lack of expertise, experience and trust. Are there other factors which will drive future demand for external assurance services?
2. Can you identify situations where external assurance might be seen as the only feasible solution to addressing the need for credible information and what are the key characteristics of such situations?
3. Do you consider that the variety of external assurance services available meets market needs or can you identify circumstances where there is a confusing variety of external assurance services and reports in the market place?
4. Are there areas where external assurance services would be useful but are not available?

### Regulation of external assurance

5. Under what conditions is regulation of external assurance necessary?
6. To what extent should regulation be provided and by whom?
7. In what areas might it be useful to have a consistent framework and set of standards on external assurance to help ensure that consistent external assurance services and reports are being provided to stakeholders?
8. In what areas do frameworks already exist and are they helpful?

### **The International Auditing and Assurance Standards Board *International Framework for Assurance Engagements* (the IAASB Framework)**

9. Can the IAASB Framework be applied in practice to a wide range of external assurance services? Please give reasons for your answer.

10. This discussion paper raises a number of issues in relation to three-party relationships, identification of users, suitable criteria, materiality, reporting and qualified, adverse and disclaimers of conclusions. Do you have any comments on the particular points raised or suggested solutions and can you identify any other issues?

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# 1. Introduction

## 1.1 Background

Information is fundamental to market activities and to determining public policy – that is, the body of policies that different members of society and organisations within it pursue in order to promote the public good. Society has an interest in the ability of these individuals or groups to be able to rely on credible information flows to make sound decisions and policy. For information to be credible, it needs to be objective, of good quality and fit for purpose. Trust and integrity are important factors that underpin credible information flows.

Policy makers might need to consider whether there are appropriate mechanisms in place to meet these information needs and to ensure that markets are not being undermined by a loss of faith in the reliability of information and to help to ensure that public policy continues to work. Historically, policy makers have often turned to professionals, such as accountants to help address concerns. Examples of such mechanisms include the involvement of professionally qualified accountants to guard against money laundering or the statutory audit, which helps to safeguard the interests of shareholders.

The statutory audit of financial statements is an example of external assurance. There are, however, other areas where external assurance services are being or could be provided, for example, on information relating to internal controls, outsourced operations and compliance with contractual agreements. The need for external assurance may be particularly evident where there are different interests at stake and where there is a need for objective information, such as reporting on environmental performance or outsourced operations. Is there, therefore, scope for extending and developing the role of external assurance?

*Information for markets and society*, a report in the Institute of Chartered Accountants in England and Wales' (ICAEW) *Information for Better Markets* campaign, provides a simple model – the Information for Better Markets Framework – for illustrating the importance of, amongst other things, external assurance in delivering the desired results of public policy.<sup>1</sup> The model is summarised in Appendix 1 and this paper draws on some of the ideas behind the model.

## 1.2 Objectives and scope of this discussion paper

This discussion paper explores the role of external assurance from a policy-making perspective and seeks to generate discussion of public interest issues relating to the provision and performance of external assurance services and to encourage further research in this area. It is aimed at policy makers and those with an interest in public policy issues and may be of particular interest to governments, non-governmental organisations (NGOs) and other interest groups, regulators, standard setters and academics.

This is one of the discussion papers in the *Perspectives on assurance* series, part of the ICAEW Audit and Assurance Faculty's *re:Assurance* initiative which promotes dialogue on assurance with interested parties. The role of external assurance in society may be influenced by the perceived benefits that business and their stakeholders may gain through external assurance and the ability of practitioners to deliver these benefits. These issues are explored separately in other discussion papers in this series. These papers seek to assist both business and practitioners in responding to potential opportunities and challenges by raising a number of practical questions and encouraging feedback based on practical experiences.

Over the last two decades there have been other initiatives in the area of external assurance, some of which have focused on the identification and promotion of new assurance services.<sup>2</sup> The objective of these papers, however, is to seek to engage with those who have an interest in reliable business information and, through discussion of the issues around the role of external assurance, to try to gain a broader understanding of the needs of business, their stakeholders and society at large.

<sup>1</sup> *Information for markets and society*, London: ICAEW, 2005.

<sup>2</sup> For example, work carried out through the American Institute of Certified Public Accountants' (AICPA) Vision Project and Special Committee on Assurance Services, see [www.cpavision.org](http://www.cpavision.org).

## 2. External assurance and society

### 2.1 A role for external assurance?

When information from business<sup>3</sup> is made publicly available, there is likely to be a number of stakeholders, such as public and voluntary bodies, investors, governments, tax authorities, market regulators, policy makers, NGOs and other interest groups that might want to use it.

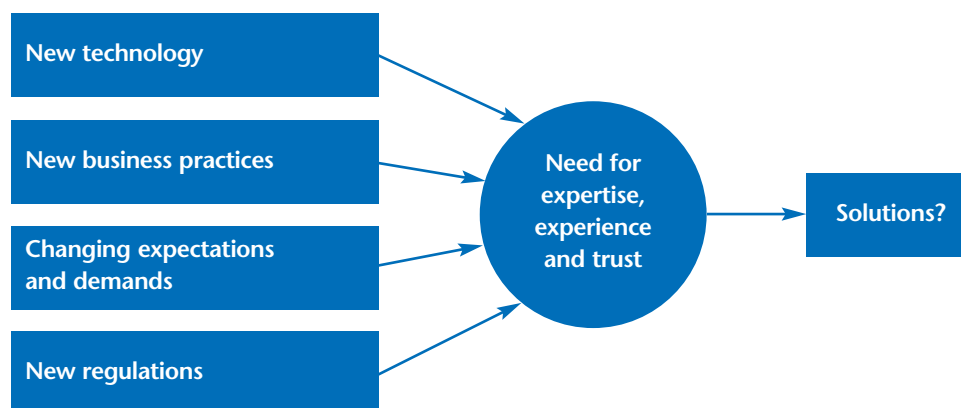
These stakeholders need to rely on credible information to make effective economic decisions and policy with confidence and society has an interest in this. Trust and integrity are important factors that underpin credible information flows. *Reporting with integrity*, a report in the ICAEW's *Information for Better Markets* campaign, explains that integrity inspires trust and is vital to the reputation of businesses.<sup>4</sup> It can, however, be difficult to build trust in today's dynamic economic environment and confidence diminishes where there is uncertainty about the reliability of information or its fitness for purpose.

There are a number of factors that might affect the reliability and usefulness of information. The business world is fast-changing and complex. Businesses must deal with new technology and business practices, changing expectations of stakeholders and demands for further information and a stream of new regulations. Similarly, globalisation and changing market expectations lead to new opportunities for businesses to work with different people and whilst these opportunities can help businesses to grow, they often call for new types of expertise and experience. Businesses might question whether they can address these issues and take advantage of new opportunities in unfamiliar areas.

Business and their stakeholders need suitable solutions to help them address their concerns in the face of uncertainty. This is highlighted in figure 2.1.

External assurance may be one such solution. An independent expert, such as a practitioner providing a written conclusion on information, can provide a signal that information is trustworthy.

FIGURE 2.1: CHALLENGES TO CREDIBILITY



<sup>3</sup> The term 'business' is used in the broadest sense of the word to encompass activities carried out by both commercial and non-commercial entities and organisations.

<sup>4</sup> *Reporting with integrity*, London: ICAEW, 2007.

## 2.2 What is external assurance?

What do we mean by external assurance? ‘A positive declaration intended to give confidence’ is a dictionary definition of the word ‘assurance’.<sup>5</sup> When applied in the context of business information, external assurance may be described as the provision of an independent opinion by an expert practitioner (such as a chartered accountant) on information prepared by one party for the benefit of another party or parties. This opinion is intended to increase confidence in the reliability of information.

It is important to emphasise the point that the opinion comes from an independent source. Stakeholders want credible information that they can trust. Objectivity and independence are therefore essential characteristics of external assurance. Practitioners who perform assurance engagements by applying the International Auditing and Assurance Standards Board *International Framework for Assurance Engagements* (the IAASB Framework) are governed by a code of ethics which includes requirements regarding independence.<sup>6</sup> The IAASB Framework is discussed in more detail in section 4.

Another important characteristic is that of professional judgement. Practitioners need to have the ability to make professional judgements that are ethical and apply relevant knowledge to specific situations. It is essential to have the ability to understand and assess the reliability of information and to have the strength of character to challenge management where concerns arise.

## 2.3 Who are the stakeholders?

Information will generally be prepared with particular stakeholders in mind (the intended users). Often practitioners give reports on information prepared by management. In such cases the client will be the management of the company but the information can still be of use to others. There may therefore be other users of information for whom the information has not been directly prepared and with whom neither the business nor practitioners have a contractual relationship.

An example of where this happens is the statutory audit of financial statements. *Audit purpose*, a paper published by the *Audit Quality Forum* in the *Fundamentals* series, highlights that, whilst the explicit purpose of the statutory audit is to provide a report to shareholders, the statutory audit is of value for many different purposes to other stakeholders.<sup>7</sup> The financial information in financial statements may be a material source of information to many stakeholders and they will derive some comfort from the fact that an audit has been performed. *Audit purpose* recognises these interests and that the audit has a clear public interest role but explains that the purpose of the statutory audit as defined in law is clear – it is for the benefit of shareholders. The interests of and comfort gained by others are seen in the paper as consequences of the audit, albeit important ones.

Similarly, where other information is made publicly available by businesses there are likely to be a number of interested third parties, many of whom will not have a direct contractual relationship with the businesses concerned. For example, a report on corporate responsibility might be of interest to a wide range of stakeholders such as potential investors, NGOs, competitors, customers, environmental organisations, employees and regulators. External assurance might give some additional comfort to these other parties that the information provided is objective and reliable.

<sup>5</sup> *Concise Oxford English Dictionary*, Oxford: Oxford University Press, 2004.

<sup>6</sup> IAASB functions as an independent standard setting body under the auspices of the International Federation of Accountants (IFAC). The ICAEW is a member body of IFAC and is committed to supporting its work.

<sup>7</sup> *Audit purpose*, London: *Audit Quality Forum*, 2006.

## 2.4 Ways of building confidence

External assurance is one of many ways in which business and their stakeholders can build trust in the reliability of information. Some businesses might believe that their internal controls and internal audit functions support credible information flows in the business or they may outsource specific operations to organisations with the relevant experience and expertise that is required, without feeling a need for external assurance. Likewise, businesses might engage directly with their stakeholders, through website tools, stakeholder forums and open days or other mechanisms, to help ensure that stakeholders' needs are being met.

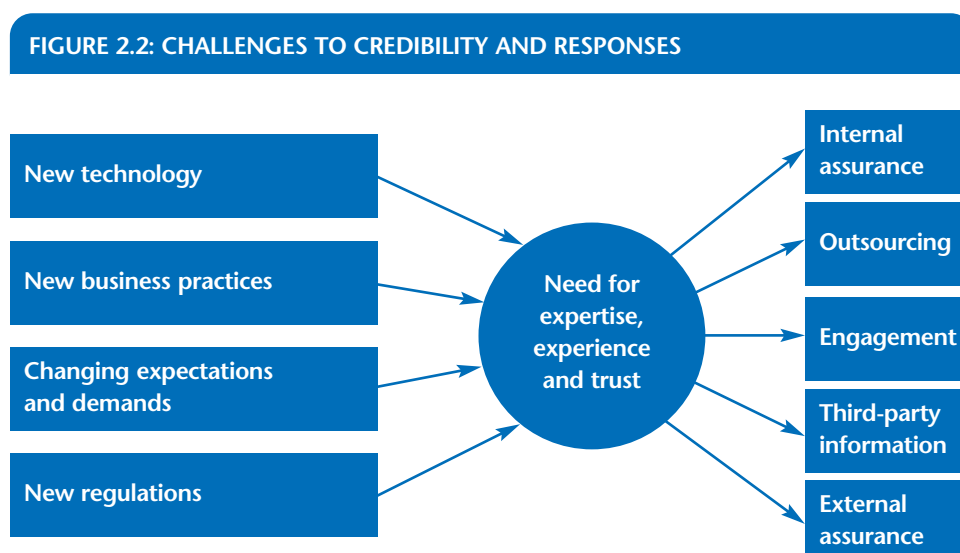
Where stakeholders meet regularly with businesses they may have the ability to demand additional information where necessary or to influence policies and decisions taken by businesses. These relationships help stakeholders gain a better understanding and knowledge of businesses and how they operate and indicate that external assurance is not the only solution available to help reinforce trust in the reliability of information.

There are, however, other external sources (third-party information) that stakeholders might use to assess the reliability of information. For example, service industries like the restaurant trade rely heavily on reputation to attract customers. Customers will use information from food critics, restaurant guides and experiences of friends and family to decide whether or not to eat in a particular restaurant. The internet also provides useful sources of information to stakeholders.

Some markets have thrived by providing people with access to reliable information. E-bay is a good example of a market that has developed and flourished by establishing trust. E-bay relies heavily on feedback from market participants about the integrity of suppliers and customers in completing transactions. Businesses might also often seek to gain credibility and enhance their reputation through gaining credentials such as awards and certificates and competitors might expose the poor quality of businesses' products or information through advertising campaigns. There are also other ways of assessing information, for example, through externally compiled industry benchmarking data.

Businesses might choose more than one solution. For example, in certain circumstances stakeholders may look for both effective internal controls and an external assurance report to meet their needs. One key difference, however, between some of the solutions outlined above and external assurance will often be independence. An external assurance service, as discussed in this paper, is carried out by an expert who satisfies published independence criteria.

Building on the model in figure 2.1 the solutions could be presented as follows:



The provision of certain services or products might be directly monitored by a regulator such as a government body or non-governmental organisation. The regulator might have in place codes of conduct, reporting requirements and other rules, which help to satisfy the information needs of stakeholders and thereby allow regulators to dispense with some form of third-party assurance. In circumstances where a need for some form of independent expert opinion is identified, this regulatory model could, however, be extended by the regulator choosing to sub-contract assurance work directly to a third party. However, such a model is not common in the UK, where businesses are generally responsible for engaging practitioners to provide an external assurance service for the benefit of stakeholders.

## 2.5 Reconciling expectations

Whilst it is clear that there are benefits to be gained from external assurance, it is not a panacea to be applied without a proper understanding of the needs and expectations of stakeholders. A wide range of stakeholders use information prepared by businesses and they may have different expectations of external assurance. It might not be possible to reconcile all these different expectations.

There are currently different external assurance reports with different forms of conclusions being provided in the market place and this lack of consistency might make it difficult to assess the benefits gained by society from external assurance. On the other hand, the fact that there are a number of different external assurance reports being provided would suggest that practices are changing to meet the needs of stakeholders and that these stakeholders do receive some valuable benefits. These reports might be satisfying different audiences for different purposes and if this is the case, the need for consistency becomes less relevant.

### QUESTIONS FOR DISCUSSION

1. This discussion paper sets out a number of factors that might influence the need for external assurance, such as new technology, business practices, changing expectations of stakeholders and demands for further information and new regulations which raise concerns about lack of expertise, experience and trust. Are there other factors which will drive future demand for external assurance services?
2. Can you identify situations where external assurance might be seen as the only feasible solution to addressing the need for credible information and what are the key characteristics of such situations?
3. Do you consider that the variety of external assurance services available meets market needs or can you identify circumstances where there is a confusing variety of external assurance services and reports in the market place?
4. Are there areas where external assurance services would be useful but are not available?

## 3. Regulation of external assurance

### 3.1 Background

External assurance plays a role in society which raise questions about the need for regulation. Even if relevant stakeholders do not perceive a need for external assurance, a requirement for external assurance may still be imposed in particular areas because it is deemed to be in the public interest and for the greater benefit of society at large. External assurance is often therefore imposed as a requirement rather than being taken on voluntarily. The statutory audit is an example of this.

Likewise, there may be circumstances where stakeholders recognise the value of external assurance and identify a need for regulation to maintain quality and to establish standards of behaviour and consistency in approach by those providing external assurance services.

External assurance reports can also be lengthy and use terminology that is difficult to understand. Expectations of business and stakeholders as to what an external assurance report does might also differ considerably from what is intended by practitioners. Markets appear to have changed and grown to try to meet the different expectations through the development of different products. Where there are clearly defined and discrete stakeholders then confusion is less likely to be an issue as comparisons between external assurance reports may not be necessary. However, if a group of stakeholders is receiving information and related external assurance in different ways then it will be difficult to make comparisons.

To reduce the potential for confusion and to aid comparability, one way forward might be to extend the regulation of external assurance, by introducing a consistent framework and standards or guidance for the performance of external assurance services applicable to all providers of assurance services. Stakeholders may not be directly interested in the detail of these standards but might still be keen to ensure that such standards exist and are being followed consistently.

The *Information for markets and society* report suggests that, for assurance to be of value, it must be conducted by people who have and are perceived to have integrity.<sup>8</sup> How do stakeholders, such as the intended users of information and related assurance reports and those other interested parties with no direct relationship with the businesses concerned, assess the integrity and quality of the practitioner providing the external assurance report without a detailed knowledge of the practitioner? Members of one of the professional bodies are already subject to a degree of regulation which covers performing external assurance services, regardless of whether or not there is an actual regulatory requirement for the external assurance service itself. Regulation could, however, be extended further through the introduction of requirements covering issues such as licensing practitioners, education, qualifications, training and continuing professional development, ethics and public oversight.

Such regulation has been witnessed in the audit market with the introduction of wide-ranging legal requirements, including specification of who can carry out such work, the development of auditing and ethical standards on how to perform an audit and oversight of the audits being performed.

It is important that any regulation introduced is sufficiently flexible to meet the needs of stakeholders. Regulation needs to be proportionate and meet the principles of better regulation. If the benefits of regulation are perceived not to justify the costs then it may lead to over-regulation which might result in, for example, more boilerplate external assurance reports which some may argue provide little value to stakeholders, and could ultimately lead to a reduction in the demand for external assurance services.

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<sup>8</sup> *Information for markets and society*, London: ICAEW, 2005.

Practitioners might also believe that the market for external assurance services operates effectively without the need for further regulation and that such regulation may result in some practitioners moving away from the provision of external assurance services.

### 3.2 Standards and frameworks on assurance

Potential confusion and expectation gaps are driving forces behind the development of consistent frameworks. Accountants may choose to follow the the IAASB Framework and International Standard for Assurance Engagements 3000, *Assurance engagements other than audits or reviews of historical financial information* (ISAE 3000) and other guidance issued by professional bodies when performing external assurance services. For example, the ICAEW has issued the following guidance which is consistent with the IAASB Framework:

- Technical Release AAF 01/06, *Assurance reports on internal controls of service organisations made available to third parties*;
- Technical Release ITF 01/07, *Assurance report on the outsourced provision of information services and information processing services*; and
- Interim Technical Release AAF 03/06, *The ICAEW assurance service on unaudited financial statements*.

The IAASB Framework is applicable to all types of assurance engagements. It is generally accepted by the accounting profession and the model used for financial statement audits performed under International Standards on Auditing (ISAs) is consistent with it. However, others providing external assurance services outside the accounting profession are not always willing or able to follow the IAASB Framework when providing external assurance services and are certainly not required to do so. Whilst there is no generally accepted standard or framework which governs external assurance services outside the accounting profession, other frameworks, standards and guidance exist in specific areas of external assurance. For example, a number of external assurance reports on corporate responsibility information refer to the AA1000 Assurance Standard issued by AccountAbility, which is founded on three sustainability assurance principles: completeness, materiality and responsiveness.

An accepted framework might help to improve consistency of reporting and reduce the level of confusion about external assurance. As more information and external assurance reports become publicly available, the demand for a consistent framework and supporting standards or guidance for external assurance services is likely to grow.

#### QUESTIONS FOR DISCUSSION

5. Under what conditions is regulation of external assurance necessary?
6. To what extent should regulation be provided and by whom?
7. In what areas might it be useful to have a consistent framework and set of standards on external assurance to help ensure that consistent external assurance services and reports are being provided to stakeholders?
8. In what areas do frameworks already exist and are they helpful?

## 4. The IAASB Framework

### 4.1 Definition and key elements of assurance engagements

The IAASB Framework sets out high-level principles applicable to various types of assurance engagement. Practitioners who perform assurance engagements by applying the IAASB Framework are governed by the International Federation of Accountants (IFAC) *Code of Ethics for Professional Accountants*.<sup>9</sup> Section 290 of the Code requires members of assurance teams, firms and, when applicable, network firms to be independent of assurance clients. These provisions are included in the ICAEW's *Code of Ethics*, the latest version of which took effect from 1 September 2006.

The IAASB Framework defines an assurance engagement as:

'An engagement in which a **practitioner** expresses a conclusion designed to enhance the degree of confidence of the **intended users** other than the **responsible party** about the outcome of the evaluation or measurement of a **subject matter** against **criteria**.'

The terms which we have highlighted in bold are defined below:

**Practitioners** – those parties who are providing the assurance service (e.g. a chartered accountant).

**Intended users** – those parties for whom the assurance report is prepared. This can include the responsible party although the responsible party cannot be the sole user of the report.

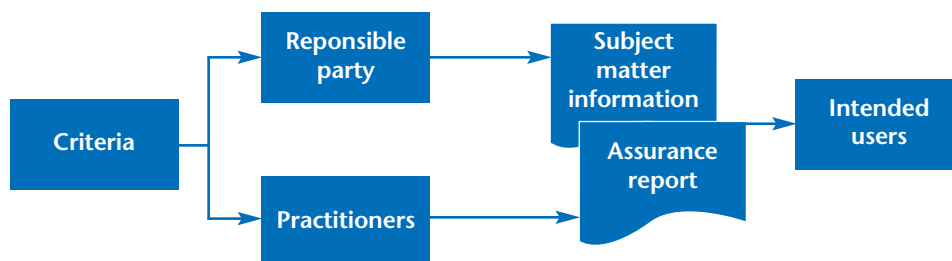
**Responsible party** – the party that is responsible for preparing and providing the information or the assertion, for example, the management of a company.

**Subject matter** (and subject matter information) – what practitioners are reporting on. Subject matter refers to underlying matter of interest to intended users and subject matter information is information that results from evaluating or measuring the subject matter.

**Criteria** – the benchmarks against which to measure the subject matter.

Figure 4.1 illustrates how these fit together for an assurance engagement.

FIGURE 4.1: DEFINITION OF AN ASSURANCE ENGAGEMENT



<sup>9</sup> *Code of Ethics for Professional Accountants*, New York: IFAC, 2005.

The key elements of an assurance engagement, as explained in the IAASB Framework, are as follows:

- a three-party relationship;
- appropriate subject matter;
- suitable criteria;
- sufficient appropriate evidence; and
- a written assurance report.

These elements are explained in more detail in *Perspectives on assurance: Engaging practitioners*.

If stakeholders consider that there is value in having a consistent framework for external assurance services then the IAASB Framework might be a valuable tool. If the IAASB Framework is to be widely used, however, it needs to be capable of application to a wide range of external assurance services. We are interested in views on this. In terms of the IAASB Framework's general application, for instance, we have identified the following issues for further consideration and research but would welcome comments on any other issues relating to the IAASB Framework.

#### 4.2 A three-party relationship

The IAASB Framework says that an assurance engagement involves three separate parties; a responsible party, intended users and a practitioner. The responsible party is responsible for the subject matter and/or the reported information, the intended users are those parties for whom the report is prepared and the practitioner provides the assurance service. This works well in the 'audit model' where the responsible party is the board of directors, the intended users are the shareholders and the practitioner is the registered auditor.

The requirement for a three-party relationship can, however, be less straightforward for non-audit situations. For instance, the management of a group company may engage practitioners to assess the operation of internal controls of its subsidiaries. In this case, the two parties are within the same group, and in fact the management is ultimately responsible for the subsidiary. The IAASB Framework adopts a pragmatic approach to this type of situation: where an organisation has a layered management structure, the board is unlikely to be involved in the controls of its subsidiaries on a day-to-day basis. In such cases, the management may benefit from the practitioners' independent assessment of the subsidiary's operations. The separation of the responsible party from the users is however often far less clear if the client is a smaller organisation.

There are clearly some circumstances in which the dual role of users and responsible parties is difficult to separate. This raises questions as to whether practitioners should take on work in such circumstances and what guidance they should follow. Is it right to restrict assurance engagements to situations where there are three-parties or should it be flexible to meet market needs?

#### 4.3 Identification of users

The identification of the users and understanding their expectations are essential for practitioners in planning the scope of any assurance engagement and the related work procedures. Consideration of the needs of users is vital in establishing what is material and minimising the expectation gap between what users want and what practitioners are providing in their assurance report.

There may, however, be users that are not known at the time of the engagement. For example there may be circumstances where, after the engagement has begun, parties outside the engagement appear claiming an interest in the information or cases where the information is prepared for a speculative audience who are yet to be determined at the time of the engagement.

This poses difficulties for practitioners as it is not possible to incorporate an infinite number of unknown stakeholders within the scope of an engagement. One way of trying to address this is to communicate the limitation on intended users in the conclusion of the assurance report but this might reduce the value of the report. Ultimately, practitioners will need to consider whether they are willing to take the risk in the circumstances and continue to do the work.

#### 4.4 Suitable criteria

An important element of an assurance engagement is the need for suitable criteria. According to the IAASB Framework, suitable criteria need to be relevant, complete, reliable, neutral and understandable. Practitioners are required to assess the suitability of criteria by considering whether they reflect these characteristics. Identifying suitable criteria might be quite difficult, however, especially in circumstances where practitioners are carrying out new types of assurance engagements where there may be no established criteria.

Can practitioners carry out such engagements? If we look back in the past, we can see that auditing existed long before the development of key criteria such as accounting standards. It may be the case that auditors might have used some other broad ideas at the time, such as norms of behaviour, coupled with professional judgement. Could this be relevant to considering the need for criteria today or has there been a shift in focus to a need to identify more detailed criteria? Suitable criteria might not necessarily mean standards. There might be scope for criteria to be more high level, but alongside a greater emphasis on the need for practitioners to use their professional judgement.

#### 4.5 Materiality

As the IAASB Framework explains, materiality is relevant when the practitioner is determining the nature, timing and extent of procedures and when assessing whether information is free of misstatement. Users' needs are the key to any decision about materiality.

Where users have been defined and consulted by the responsible party, practitioners are likely to find it easier to understand and assess the factors that might influence their decisions. If no consultation has taken place or there are too many users, then practitioners will need to use their professional judgement to determine what will affect the users' decision making and whether they have enough information to be able to reach a conclusion. This may be especially difficult where practitioners are reporting on non-financial information. To help them in their judgement, practitioners might, for instance, choose to use the concept of 'reasonable man (or person)' as used in common law.

#### 4.6 Reporting

The IAASB Framework requires practitioners to provide a written report with a conclusion conveying the assurance obtained about the information that is being reported on. The IAASB Framework and ISAE 3000 do not prescribe standardised wording but identify the basic elements that the report should include.

In terms of the conclusion, according to the IAASB Framework there are only two types of assurance engagement: reasonable assurance and limited assurance. The difference between these types of assurance is reflected in the nature of the work performed, the level of engagement risk, and the type of conclusion provided. A reasonable assurance report

contains a positive conclusion whereas a limited assurance conclusion is expressed in a negative form, i.e. 'nothing has come to our attention that causes us to believe that XYZ is not fairly stated'. Put simply, limited assurance engagements seek to provide a lower level of comfort to users than reasonable assurance engagements. Some may argue that the definition of the types of assurance engagement is too ambiguous and gives too much flexibility in its interpretation. Others may, however, say that this streamlines the type of assurance conclusion in the market place and, as a result, can restrict flexibility.

The IAASB Framework only refers to reasonable assurance engagements or limited assurance engagements. Whilst separate conclusions might be provided on different aspects of the information prepared by the responsible party, there does not seem to be an option to carry out an engagement that has both reasonable assurance and limited assurance aspects within a single report. Some argue that this limits flexibility but others say that the type of assurance within a report which obviously relates to a single engagement should be consistent to prevent expectation gaps.

#### 4.7 Qualified, adverse and disclaimers of conclusions

If practitioners cannot express an unqualified conclusion then the IAASB Framework explains that the practitioner might need to give a qualified conclusion, an adverse conclusion or a disclaimer of conclusion. They might also need to consider whether they should withdraw from the engagement. Where there is a limitation on the scope of the practitioners' work, they would either issue a qualified conclusion or disclaimer of conclusion depending on how pervasive the limitation of scope is. Where the subject matter is materially misstated or where the responsible party's assertion is not fairly stated then practitioners will need to issue a qualified or adverse conclusion. An example of a qualified conclusion is 'except for [the particular issued identified], XYZ is fairly stated'. An example of an adverse conclusion is that 'XYZ is not fairly stated'.

We are interested in identifying any other potential conclusions or information that could be given in these circumstances, other than just qualifying the report, that might be more informative and add value to users.

A question that arises is whether qualifications should be used in limited assurance engagements as well as in a reasonable assurance engagement because by their very nature they already only provide a negative conclusion and so the level of comfort is already restricted. Qualification of a limited assurance conclusion might make it difficult for users to understand the level of assurance obtained by practitioners.

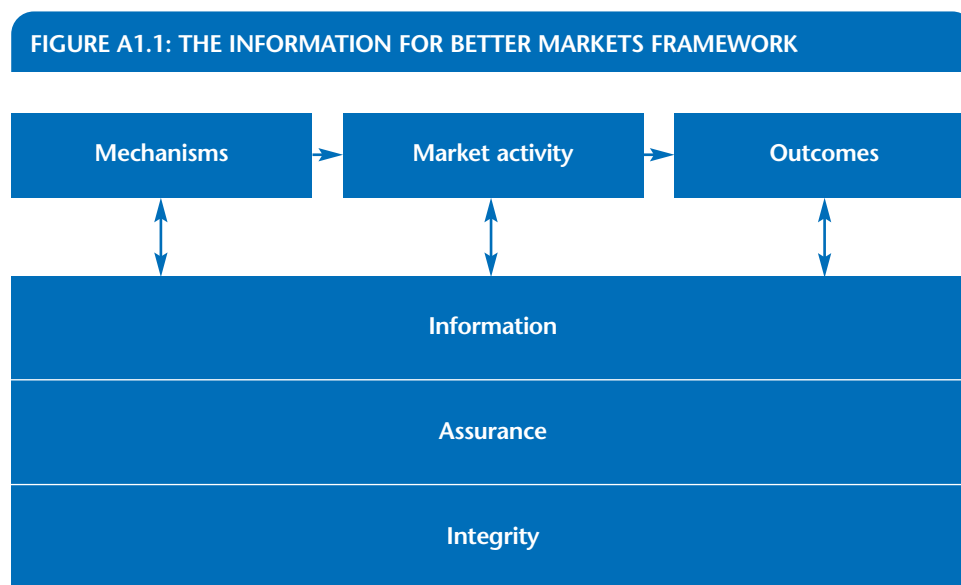
#### QUESTIONS FOR DISCUSSION

9. Can the IAASB Framework be applied in practice to a wide range of external assurance services? Please give reasons for your answer.
10. This discussion paper raises a number of issues in relation to three party relationships, identification of users, suitable criteria, materiality, reporting and qualified, adverse and disclaimers of conclusions. Do you have any comments on the particular points raised or suggested solutions and can you identify any other issues?

## Appendix 1 – The role of assurance in public policy

A report in the ICAEW's *Information for Better Markets* campaign, *Information for markets and society*, sets out a way of approaching public policy issues that stresses the role of information in the design, implementation and assessment of public policy.

*Information for markets and society* provides a simple model – the Information for Better Markets Framework – for illustrating the importance of integrity, assurance and information for guiding mechanisms and market activity towards the achievement of desired outcomes. This is illustrated below.



**Outcomes** are desired results of public policy, such as improving people's health or education or national economic performance, or protecting the environment, or reducing crime. The desired outcomes of public policy are usually achieved through lower level subordinate outcomes, which are in turn achieved through outcomes at a yet lower level, and so on. Potentially this process can go on ad infinitum, but in practice it is usually sufficient to trace outcomes down through no more than a few levels.

**Mechanisms** are the means that society employs to promote the outcomes that it desires. Mechanisms are ways of persuading, requiring or incentivising individuals to change their behaviour. They include corporate policies, supply chain pressure, stakeholder engagement, voluntary codes, rating and benchmarking, taxes and subsidies, tradable permits and requirements and prohibitions.

**Market activity** in this context is a term used to describe all the activities of individuals and organisations that lead to the achievement (or non-achievement) of desired outcomes.

**Information** influences and is itself influenced by mechanisms, market activity and desired outcomes. This feedback loop in turn affects the design of mechanisms, market activity and the specification of market outcomes. Information also provides evidence as to whether desired outcomes have been achieved. If desired outcomes have not been achieved, this may cause mechanisms to be changed in order to guide market activity towards the attainment of desired outcomes. Alternatively, the specification of the desired outcomes may change.

However, the ability of markets and public policy to deliver desired outcomes is dependent on society's ability to rely on high quality information which in turn needs to be prepared and reported by people and organisations who have and are perceived to have **integrity**. At times, the reliability of information can be enhanced by objective and independent verification from a third party, that is, **assurance**. However, for assurance to be of value, it must also be conducted by people who have and are perceived to have integrity.

## Appendix 2 – References

### Accountability

AA1000 Assurance Standard, 2003  
[www.accountability21.net/aa1000/](http://www.accountability21.net/aa1000/)

### Audit Quality Forum

*Audit Purpose*, 2006  
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*Reporting with integrity*, 2007  
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### International Auditing and Assurance Standards Board

*International Framework for Assurance Engagements*, 2004  
[www.ifac.org/Guidance](http://www.ifac.org/Guidance)

International Standard for Assurance Engagements 3000, *Assurance engagements other than audit or reviews of historical financial information*, 2004  
[www.ifac.org/Guidance](http://www.ifac.org/Guidance)

### International Federation of Accountants

*Code of Ethics for Professional Accountants*, 2005  
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December 2007