

IAASB CAG PAPER



International Federation of Accountants

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Agenda Item B.5.2

Committee: IAASB Consultative Advisory Group

Meeting Location: Basel

Meeting Date: March 3-4, 2008

Report Back—Service Organizations (ISAE 3402)

Objectives of Agenda Item

1. The objective of this Agenda Item is to provide a brief report back on the proposals of Representatives on the “first read” draft of ISAE 3402, “Assurance Reports on a Service Organization’s Controls ” discussed at the September 20-21 2007 CAG meeting.
2. The IAASB approved an exposure draft (ED) of this proposed ISAE at its December 2007 meeting.

Report Back – September 20-21, 2007 CAG Proposals

3. Below are extracts from the minutes of the September 20-21, 2007 CAG meeting¹ related to the discussions of draft ISAE 3402, and an indication of how the IAASB Task Forces or the IAASB responded to the Representatives’ comments.

Representatives’ Comments	IAASB Task Force/IAASB response
The Representatives commented as follows:	
<ul style="list-style-type: none">• Mr. Roussey supported the approach in proposed ISAE 3402 that the service organization should take responsibility for the description and make published assertions about the fair presentation of that description, the proper design of controls, and the operating effectiveness of controls. Ms. Blomme also supported the assertion-based approach.	The Task Force and the IAASB agreed to adopt this approach, and to also seek the views of respondents specifically on it. Refer to the discussion of “Assertion-based Engagements” at page 6, and question 1 at page 9, of the Explanatory Memorandum accompanying [proposed] ISAE 3402
<ul style="list-style-type: none">• Mr. Sekiguchi asked whether this approach will result in a different level of assurance.	As the meeting, Mr. Tucker responded that the level of assurance would be the same, i.e., “reasonable assurance,” which matches the evidence requirements of proposed ISA 402.

¹ The minutes will be approved at the March 2008 IAASB CAG meeting.

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Representatives' Comments	IAASB Task Force/IAASB response
<ul style="list-style-type: none"> Mr. Roussey supported the approach in proposed ISAE 3402 that the auditor's report should be worded in terms of the underlying subject matter, rather than in terms of the service organization's assertions. Ms. Blomme also supported the wording of the service auditor's report. 	<p>The Task Force and the IAASB agreed to adopt this approach. Refer to paragraph 56(j) of [proposed] ISAE 3402</p>
<ul style="list-style-type: none"> Mr. Scicluna asked whether the issue of a "dirty assertion" could arise for all conclusions within the service auditor's report. A "dirty assertion" is where the service organization correctly asserts that, e.g., controls are not operating effectively; and the auditor's opinion states that this assertion is correct. 	<p>At the meeting, Messrs. Tucker and Nugent explained that, under the proposed approach, any modification is explained in one paragraph, which includes the explanation of its effects. The opinion paragraph, which includes all three opinions, is then introduced with a single "except for" (or other relevantly worded caveat).</p>
<ul style="list-style-type: none"> Mr. Morris asked why this model of expressing modifications is being used, noting that it differs from the USA and Canadian model. 	<p>At the meeting, Mr. Tucker responded that, where the reason for a modification is related to more than one of the opinions, which is often the case, the USA and Canadian model can present unnecessary difficulties for the service auditor in trying to separately explain the effect on each of the three opinions, and the result can be unnecessarily confusing for the reader. He also noted that the proposal would provide the same information to users that they are receiving under the present USA and Canadian model.</p>
<ul style="list-style-type: none"> Mr. Morris asked how this will affect convergence with the USA. Mr. Ray noted that the PCAOB has not made any decisions (tentative or otherwise) on this matter as yet, and it is not a priority to do so at the moment. 	<p>At the meeting, Mr. Tucker responded that the Auditing Standards Board of the American Institute of Certified Public Accountants is likely to change to the IAASB model when it is approved.</p>
<ul style="list-style-type: none"> Ms. Blomme noted that the criteria detailed in proposed ISAE 3402 may need further work. Mr. Tucker noted that the criteria were expected to be discussed in detail at the September IAASB meeting. 	<p>The criteria were considerably re-worked prior to exposure. Also, the views of respondents on this issue have been sought. Refer to the discussion of "Suitable Criteria" at page 7, and question 4 at page 9, of the Explanatory Memorandum accompanying [proposed] ISAE 3402</p>

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Representatives' Comments	IAASB Task Force/IAASB response
<ul style="list-style-type: none"> Ms. Wood noted that, in a group audit, the group engagement team cannot automatically rely on the component and that, in a sense, a service auditor's report on that part of the system covered by the service organization is similar to a component audit. She asked how this analogy relates to proposed ISAE 3402. 	<p>At the meeting, Mr. Tucker responded that the audit of the user organization is performed in accordance with proposed ISA 402, which includes relevant considerations for the user auditor, including evidence considerations in using an "ISAE 3402 report."</p>
<ul style="list-style-type: none"> Mr. Morris asked whether the Task Force prefers Type A or Type B reports. Mr. Tucker responded that the Task Force sees only limited application for Type A reports – primarily when the service organization has not been in operation long enough to have a track record that allows for a Type B. Mr. Morris suggested that this be made clearer in proposed ISAE 3402. It was noted that ISA 402 has material to assist the user auditor with how to use Type A and Type B reports. Mr. Roussey agreed with Mr. Morris and suggested that Type A reports could perhaps be dealt with in an appendix, thus ensuring that prominence is given to Type B reports. 	<p>The Task Force and the IAASB agreed: that the example Type A report would include the statement "We did not perform any procedures regarding the operating effectiveness of controls included in the description, and accordingly do not express an opinion thereon;" to give Type B reports prominence by referring to them first in sentences where both Type A and Type B reports are mentioned (e.g., para 56(c)(i)); and, to discuss the distinction between Type A and Type B reports the Explanatory Memorandum. <i>Refer to the discussion of "Type of Report" at page 5 of the Explanatory Memorandum accompanying [proposed] ISAE 3402</i></p>
<ul style="list-style-type: none"> Mr. Roussey suggested there could be more examples of IT controls because service organizations often use IT. He noted that a generic IT control framework could also be mentioned, perhaps in an appendix and offered assistance in this regard, should the Task Force wished to pursue this idea. Mr. Tucker responded that the Task Force has discussed whether it should attempt to develop specific controls and had decided against it, but will reconsider. 	<p>The Task Force and the IAASB agreed not to include examples of controls and control objectives, including IT controls, in the draft, but have raised this as a significant matter for consideration by respondents. <i>Refer to the discussion of "Control Objectives" at page 5 of the Explanatory Memorandum accompanying [proposed] ISAE 3402.</i></p>
<ul style="list-style-type: none"> Mr. Peyret, who was unable to attend the meeting, had e-mailed comments on this item which will be passed to the Task Force. Mr. Roussey noted that these comments deal mostly with Shared Service Centers (SSCs), and asked whether the Task Force has considered whether proposed 	<p>At the meeting, Mr. Tucker explained that nothing precludes application of the proposed ISAE to SSCs. However, addressing SSCs directly would make the proposed ISAE unduly complicated because of the need to link it with ISA 600 (Revised and Redrafted), "Special Considerations – Audits of Group Financial</p>

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ISAE 3402 should apply to SSCs.	Statements (Including the Work of Component Auditors)."

Material Presented – FOR IAASB CAG REFERENCE PURPOSES ONLY

Available from
<http://www.ifac.org/Guidance/EXD-Details.php?EDID=0099>

Exposure Draft of Proposed ISAE 3402,
“Assurance Reports on Controls at a Third Party
Service Organization” published in December 2007