

ISSAI 200

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INTOSAI



Fundamental Principles of Financial Auditing

INTOSAI



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INTRODUCTION

1. Professional standards and guidelines are essential for the credibility, quality and professionalism of public-sector auditing. The International Standards of Supreme Audit Institutions (ISSAIs) developed by the International Organisation of Supreme Audit Institutions (INTOSAI) aim to promote independent and effective auditing and support the members of INTOSAI in the development of their own professional approach in accordance with their mandates and with national laws and regulations.
2. *ISSAI 100 – Fundamental Principles of Public-Sector Auditing* provides the fundamental principles for public-sector auditing in general and defines the authority of the ISSAIs. *ISSAI 200 – Fundamental Principles of Financial Auditing* has been developed to address the key principles related to an audit of financial statements in the public sector. It builds on and further develops the fundamental principles of ISSAI 100 to suit the specific context of audits of financial statements, and constitutes the basis for auditing standards related to audits of financial statements. ISSAI 200 should be read and understood in conjunction with ISSAI 100.
3. The main purpose of the ISSAIs on financial audit is to provide INTOSAI members with a comprehensive set of principles, standards and guidelines for the audit of financial statements of public-sector entities. In addition to ISSAI 200, the ISSAIs on financial audit comprise the Financial Audit Guidelines (ISSAIs 1000-2999) at level 4 of the ISSAI Framework. A general introduction to these guidelines is given in ISSAI 1000, while ISSAIs 1200 to 1810 each contain *Practice Notes* issued by INTOSAI to provide guidance on the application of the International Standards on Auditing (ISAs 200 to 810) developed by the International Auditing and Assurance Standards Board (IAASB). Each Practice Note and the corresponding ISA together constitute a guideline in the ISSAI Framework.
4. Financial audit focuses on determining whether an entity's financial information is presented in accordance with the applicable financial reporting and regulatory framework. The scope of financial audits in the public sector may be defined by the SAI's mandate as a range of audit objectives in addition to the objectives of an audit of financial statements prepared in accordance with a financial reporting framework. These objectives may include the auditing of:
 - states' or entities' accounts or other financial reports, not necessarily prepared in accordance with a general-purpose financial reporting framework;
 - budgets, budget sections, appropriations and other decisions on the allocation of resources, and the implementation thereof;
 - policies, programmes or activities defined by their legal basis or source of financing;
 - legally-defined areas of responsibility, such as the responsibilities of ministers; and
 - categories of income or payments or assets or liabilities.

5. When the SAI's mandate defines such additional audit objectives, the SAI may also need to consider developing or adopting standards based on the general fundamental principles of public-sector auditing in ISSAI 100 and the fundamental principles of compliance and performance auditing. The guidance of the Financial Audit Guidelines on special-purpose frameworks¹, audits of single financial statements and specific elements, accounts or items of a financial statement², and reports on summary financial statements³, may also be relevant for such purposes.
6. This ISSAI provides detailed information on the following:
 - The purpose and authority of the Fundamental Principles of Financial Auditing
 - The framework for auditing financial statements in the public sector
 - The elements of an audit of financial statements
 - The principles of an audit of financial statements.

PURPOSE AND AUTHORITY OF THE FUNDAMENTAL PRINCIPLES OF FINANCIAL AUDITING

7. ISSAI 200 provides the fundamental principles for an audit of financial statements prepared in accordance with a financial reporting framework. The principles also apply when an SAI is engaged or has responsibility to audit single financial statements and specific elements, accounts or items of a financial statement, or financial statements prepared in accordance with special-purpose financial frameworks, or summary financial statements. Where reference is made in ISSAI 200 to audits of financial statements, this includes responsibilities of this nature.
8. ISSAIs 1000 to 1810 on financial audits may be applied as appropriate to these responsibilities. However, auditors are prohibited from making reference to the use of the ISSAIs if:
 - the preconditions for an audit in accordance with the ISSAIs on financial audit are not in place⁴; or
 - the auditor is not able to comply with the authority attached to the ISAs⁵ and ISSAIs.
9. The Fundamental Principles of Financial Auditing apply to all public-sector audits of financial statements, whether for the whole of government, parts of government or single entities.
10. *ISSAI 200 – Fundamental Principles of Financial Auditing* represents the core of the detailed auditing standards provided by ISSAIs 1000 to 1810 at level 4 of the ISSAI Framework. The principles in ISSAI 200 can be used in three ways:

¹ ISSAI 1800 – Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks.

² ISSAI 1805 – Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement.

³ ISSAI 1810 – Engagements to Report on Summary Financial Statements.

⁴ ISSAI 1210 – Agreeing the Terms of Audit Engagements, paragraphs 6-8.

⁵ ISSAI 1000, paragraphs 37-43.

- as a basis on which to develop standards,
- as a basis on which to adopt consistent national standards,
- as a basis for adoption of the Financial Audit Guidelines as the authoritative standards.

11. Reference to ISSAI 200 in reports should only be made if auditing standards have been developed or adopted that fully comply with all relevant principles of ISSAI 200. A principle is considered relevant when it deals with the type of audit or combinations of audit types and the circumstances or procedures are applicable. The principles in no way override national laws, regulations or mandates.
12. When adopting or developing audit standards based on the Fundamental Auditing Principles, reference to these in reports may be made by stating:

... We conducted our audit in accordance with [standards], which are based on [or consistent with] the Fundamental Auditing Principles (ISSAIs 100-999) of the International Standards of Supreme Audit Institutions.

13. SAIs adopting the Financial Audit Guidelines on level 4 as their authoritative standards should make reference to these in their reports. Depending on the standards applied and the SAI's mandate, this can be done in two ways:
- a) In accordance with ISSAIs 1000-1810 – this means full compliance with all relevant ISAs and the additional guidance set out in the INTOSAI Practice Notes;
 - b) In accordance with the ISAs – this entails compliance with all relevant ISAs.

ISSAI 100 further explains the authority attached to the ISSAIs.

14. When the level 4 ISSAIs are used as authoritative standards, the public-sector auditors should also respect the authority of the ISAs. SAIs are encouraged to strive towards full adoption of the level 4 guidelines as their authoritative standards, as they have been developed to reflect best practice. INTOSAI recognises that in some environments this might not be possible due to the absence of basic administrative structures or because laws or regulations do not establish the same premises for carrying out audits of financial statements in accordance with the Financial Audit Guidelines. Where this is the case, SAIs have the option of developing authoritative standards based on the Fundamental Principles of Financial Auditing.
15. When the level 4 ISSAIs are used as the authoritative standards for an audit of financial statements conducted together with a compliance audit, the public-sector auditors should respect the authority of both the Financial Audit Guidelines and the Compliance Audit Guidelines⁶.

⁶ ISSAI 4000 – General Introduction to Guidelines on Compliance Audit and ISSAI 4200 – Compliance Audit Guidelines Related to Audit of Financial Statements.

FRAMEWORK FOR FINANCIAL AUDITING

The objective of financial auditing

16. The purpose of an audit of financial statements is to enhance the degree of confidence of intended users in the financial statements. This is achieved through the expression of an opinion by the auditor as to whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework, or – in the case of financial statements prepared in accordance with a fair presentation financial reporting framework – whether the financial statements are presented fairly, in all material respects, or give a true and fair view, in accordance with that framework. Laws or regulations binding public-sector audit organisations may prescribe other wordings for this opinion. An audit conducted in accordance with standards based on the INTOSAI Fundamental Principles of Financial Auditing and relevant ethical requirements will enable the auditor to express such an opinion.
17. ISSAI 200 is based on the following objectives, as defined in ISSAI 1200⁷:

In conducting an audit of financial statements, the overall objectives of the auditor are:

- a) To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and
- b) To report on the financial statements, and communicate the result of the audit, in accordance with the auditor's findings.

Public-sector applications covered by ISSAI 200

Preconditions for an audit of financial statements in accordance with the ISSAIs

18. **The auditor should assess whether the preconditions for an audit of financial statements have been met.**
19. A financial audit conducted in accordance with the ISSAIs is premised on the following conditions:
- The financial reporting framework used for preparation of the financial statements is deemed to be acceptable by the auditor.
 - The management of the entity acknowledges and understands its responsibility:
 - For preparation of the financial statements in accordance with the applicable financial reporting framework, including, where relevant, their fair presentation;

⁷ ISSAI 1200, paragraph 11 of ISA 200.

- For such internal control that management deems necessary for the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
 - To provide the auditor with unrestricted access to all information of which it is aware and that is relevant to the preparation of the financial statements.
20. Financial reporting frameworks may be for general use or specific use. A framework designed to meet the information needs of a wide range of users is referred to as a general-purpose framework, while special-purpose frameworks are designed to meet the specific needs of a specific user or group of users. Frameworks may also be referred to as fair presentation frameworks or compliance frameworks. A fair presentation framework requires compliance with the framework but allows, explicitly or implicitly, that it may be necessary to depart from a requirement or to provide additional information in order to achieve fair presentation of the financial statements. The term compliance framework is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and does not acknowledge the possibility of such deviations to achieve a fair presentation.
21. Without an acceptable financial reporting framework, the management will have no appropriate basis for preparing the financial statements and the auditor no suitable criteria for auditing them. Suitable criteria should be formal. For example, in the preparation of financial statements the criteria may be the International Public Sector Accounting Standards (IPSASs), the International Financial Reporting Standards (IFRSs), or other international or national financial reporting frameworks for use in the public sector.
22. A complete set of financial statements for a public-sector entity, when prepared in accordance with a financial reporting framework for the public sector, normally consists of:
- a statement of financial position;
 - a statement of financial performance;
 - a statement of changes in net assets/equity;
 - a cash flow statement;
 - a comparison of budget and actual amounts – either as a separate additional financial statement or as a reconciliation;
 - notes, comprising a summary of significant accounting policies and other explanatory information.
 - In certain environments a complete set of financial statements may also include other reports, such as reports on performance and appropriation reports.

If the financial statements are prepared in accordance with a framework for other accounting bases, such as modified accrual or a cash basis, a complete set of financial statements may not include all of the above.

23. Frameworks prescribed by law or regulation will often be deemed acceptable by the auditor. However, even if deemed unacceptable, such a framework may be allowable if:
- the management agrees to provide the necessary additional disclosures in the financial statements to avoid their being misleading; and
 - the auditor's report on the financial statements includes an Emphasis of Matter paragraph drawing users' attention to such additional disclosures.

If the above conditions are not met, the auditor should evaluate the effect of the misleading nature of the financial statements on the auditor's report and the opinion, and consider the need to inform the legislature about the matter.

24. Acceptable financial reporting frameworks normally exhibit certain attributes that ensure that the information provided in the financial statements is of value to the intended users:
- Relevance – the information provided in the financial statements is relevant to the nature of the audited entity and the purpose of the financial statements;
 - Completeness – no transactions, events, account balances or disclosures that could affect conclusions based on the financial statements are omitted;
 - Reliability – the information provided in the financial statements:
 - (i) where applicable, reflects the economic substance of events and transactions and not merely their legal form; and
 - (ii) results, when used in similar circumstances, in reasonably consistent evaluation, measurement, presentation and disclosure;
 - Neutrality and objectivity – the information in the financial statements is free from bias;
 - Understandability – the information in the financial statements is clear and comprehensive and not open to significantly diverse interpretations.

Appendix 2 to ISSAI 1210⁸ may provide further assistance for the auditor in determining whether the financial reporting framework is acceptable.

25. In some public-sector audit environments, financial audits are referred to as budget execution audits, which often include the examination of transactions against the budget for compliance and regularity issues. Such audits may be undertaken on a risk basis or with the aim of covering all transactions. In such audit environments there is often no acceptable financial reporting framework. The results of financial transactions may be presented as a comparison between expenditure amounts and budgetary amounts. In environments where such audits are undertaken and there are no financial statements presented in accordance with an acceptable financial reporting framework, the auditor may conclude that the preconditions for an audit established by the ISSAIs on financial audit are not in place. Auditors may thus consider developing standards using the Fundamental Principles of Financial Auditing as guidance to suit their specific needs. Where the audit mandate refers to financial audit but does not link this to financial statements prepared in accordance with a financial reporting framework, it is proposed that the ISSAIs be considered best available practice and the spirit of the ISSAIs be implemented through standards devised for the specific environment. Where the audit mandate refers to audits of single financial statements and specific elements, accounts or items of a financial statement, ISSAI 1805⁹ may be relevant.

⁸ ISSAI 1210 – Agreeing the Terms of Audit Engagements.

⁹ ISSAI 1805 – Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement.

26. The type of audit performed in environments where compliance with authorities is the main focus of the audit would normally be considered a compliance audit. *ISSAI 400 – Fundamental Principles of Compliance Auditing* may be a relevant source of information for the development or adoption of standards for the audit work. If, on the other hand, the audit mandate allows for a change in audit procedures and the use of acceptable financial reporting frameworks is introduced for the preparation of financial statements, the ISSAIs on financial auditing may be adopted subsequently.

Audits of financial statements prepared in accordance with special-purpose frameworks

27. The principles of ISSAI 200 are applicable to audits of financial statements prepared in accordance with both general-purpose and special-purpose frameworks. In addition to preparing general-purpose financial statements, a public-sector entity may prepare financial statements for other parties (such as governing bodies, the legislature or other parties with an oversight function), which may require financial statements tailored to meet their specific information needs. In some environments financial statements of this kind are the only financial statements prepared by the public-sector entity. Financial statements prepared for a special purpose are not appropriate for the general public. Auditors should, therefore, carefully examine whether the financial reporting framework is designed to meet the financial information needs of a wide range of users (general-purpose framework) or of specific users, or the requirements of a standard-setting body.
28. Special-purpose frameworks relevant to the public sector may include:
- the cash receipts and disbursements basis of accounting for cash flow information that an entity may be required to prepare for a governing body;
 - the financial reporting provisions established by an international funding organisation or mechanism;
 - the financial reporting provisions established by a governing body, the legislature or other parties that perform an oversight function to meet the requirements of that body; or
 - the financial reporting provisions of a contract, such as a project grant.
29. The principles of ISSAI 200 are relevant for audits of financial statements prepared in accordance with such frameworks. In addition to these principles, SAIs may find it useful, when developing or adopting standards based thereon, to consider the requirements and guidance in ISSAI 1800, which deals with special considerations in the application of ISSAIs 1200-1700 to an audit of financial statements prepared in accordance with a special-purpose framework.

Audits of single financial statements and specific elements, accounts or items of a financial statement

30. The principles of ISSAI 200 are also applicable to audits of public-sector entities that prepare financial information, including single financial statements or specific elements, accounts or items of a financial statement, for other parties (such as governing bodies, the legislature or other parties with an oversight function). Such information may come under the audit mandate of the SAI. Auditors may also be engaged to audit single financial statements, or specific elements, accounts or items – such as projects financed by the government – although they are not engaged to audit the complete set of financial statements of the entity concerned.

31. SAIs may also find it useful to consider the requirements and guidance in ISSAI 1805 when developing or adopting standards based on the principles in ISSAI 200. ISSAI 1805 deals with special considerations in the application of the requirements of the ISAs to an audit of a single financial statement or of a specific element, account or item of a financial statement. The single financial statement or the specific element, account or item of a financial statement may be prepared in accordance with a general-purpose or special-purpose framework.

ELEMENTS OF FINANCIAL AUDITING

32. Audits of financial statements are defined as assurance engagements, which involve at least three separate parties: an auditor, a responsible party and intended users. The elements of public-sector auditing are described in ISSAI 100¹⁰. ISSAI 200 covers additional aspects of the elements relevant to an audit of financial statements.

The three parties in financial auditing

33. In an audit of financial statements, the responsible party is responsible for the subject matter information (normally the financial statements themselves) and may also be responsible for the underlying subject matter (the financial activities reflected in the financial statements). The responsible party is normally the executive branch of government and/or its underlying hierarchy of public-sector entities responsible for the management of public funds, the exercise of authority under the control of the legislature, and the content of the financial statements. These bodies are expected to manage resources and exercise authority in accordance with the decisions and premises of the legislature.
34. Legislators represent the citizens, who are the ultimate users of financial statements in the public sector. The “intended user” is primarily the parliament, which represents the citizens by making decisions and determining the priorities of public finance and the purpose and content of spending and income as part of a public democratic process. The legislature’s decisions and premises may form the basis of the broader perspective of financial audit in the public sector. For public-sector entities, legislators and regulators are often the primary users of their financial statements.
35. The responsible party and the intended users may be from the same public-sector entities or from different bodies. In the first scenario, the supervisory board of a governmental structure may seek assurance about information provided by the management board of the same public-sector entity. The relationship between the responsible party and the intended users needs to be viewed within the context of the specific engagement and may differ from more traditionally-defined lines of responsibility.

¹⁰ ISSAI 100 – Fundamental Principles of Public-Sector Auditing.

Suitable criteria

36. Criteria are the benchmarks used to evaluate or measure the subject matter, including, where relevant, benchmarks for presentation and disclosure. The criteria used in the preparation of financial statements are normally formal and may be IPSASs, IFRSs or other national financial reporting frameworks for use in the public sector.

Subject matter information

37. The financial position, financial performance, cash flows and notes presented in the financial statements (subject matter information) result from applying a financial reporting framework for recognition, measurement, presentation and disclosure (criteria) to a public-sector entity's financial data (subject matter). The term “subject matter information” refers to the outcome of the evaluation or measurement of the subject matter. It is on the subject matter information (e.g. the entity's financial statements) that the auditor gathers sufficient appropriate audit evidence to provide a reasonable basis for expressing an opinion in the auditor's report.

Reasonable assurance engagement

38. Audits of financial statements conducted in accordance with the ISSAIs are reasonable assurance engagements. Reasonable assurance is high, but not absolute, given the inherent limitations of an audit, the result of which is that most of the audit evidence obtained by the auditor will be persuasive rather than conclusive. In general, reasonable assurance audits are designed to result in a conclusion expressed in a positive form, such as “in our opinion the financial statements present fairly, in all material respects (or give a true and fair view of) the financial position of ... and its financial performance and cash flows ...” or, in the case of a compliance framework, “in our opinion the financial statements are prepared, in all material respects, in accordance with ...”.
39. Limited assurance engagements, such as review engagements, are not covered at present by the ISSAIs on financial audits. Such engagements provide a lower level of assurance than reasonable assurance engagements, and are designed to result in a conclusion expressed in a negative form, such as “nothing has come to our attention that would cause us to believe that the financial statements were not presented fairly in all material respects”. Auditors performing such engagements may need to apply guidance from outside the financial audit ISSAIs; the fundamental auditing principles in ISSAI 100 may be useful in this regard.

PRINCIPLES OF FINANCIAL AUDITING*General principles**Prerequisites for conducting financial audits*Ethics and independence

40. **The auditor should comply with the relevant ethical requirements, including those pertaining to independence, when carrying out audits of financial statements.**

41. Auditors conducting audits in accordance with the ISSAIs are subject to *ISSAI 30 – Code of Ethics* as applied in the national context. Auditors at SAIs that have adopted the level 4 ISSAIs as their authoritative standards, or that apply the ISAs, are required either to comply with the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA) (the IESBA Code), which establishes fundamental ethical principles for professional accountants, or to adopt national requirements that are at least as demanding; the INTOSAI Code of Ethics applied in the national context may be relevant here. SAIs must therefore adopt the ethical requirements of ISSAI 30 or the IESBA Code in their environment in order to be able to state in their reports that the audit was conducted in accordance with the ISSAIs or the ISAs.

Quality control

42. **The auditor should implement quality control procedures at the engagement level that provide reasonable assurance that the audit complies with professional standards and the applicable legal and regulatory requirements, and that the auditor’s report is appropriate in the circumstances.**
43. As stated in ISSAI 100, SAIs should adopt quality control procedures in accordance with *ISSAI 40 – Quality Control for SAIs*, which provides the context for the IAASB’s International Standards on Quality Control (ISQC 1) in a public-sector environment. ISQC 1 establishes standards and provides guidance for an organisation’s system of quality control. Although the general purpose and key principles of ISSAI 40 are consistent with ISQC 1, the requirements of ISSAI 40 have been adapted to ensure they are relevant to SAIs.
44. The Head of the SAI or the equivalent collective body has overall responsibility for introducing and maintaining quality control procedures in the SAI, although day-to-day operational responsibility may be delegated to others. For example, any lead auditor with responsibility for an audit engagement would ultimately report to the Head of the SAI.
45. Public-sector auditors engaged on audits of financial statements in accordance with standards based on or consistent with the principles of ISSAI 200 are subject to quality control requirements at the engagement level. When developing standards based on ISSAI 200 or adopting standards consistent with ISSAI 200, SAIs should consider formulating requirements related to:
- the need for the lead auditor to take responsibility for overall quality in each audit engagement;
 - the need for the lead auditor to ensure that members of the audit team comply with the relevant ethical requirements;
 - the need for the lead auditor to form a conclusion regarding compliance with the independence requirements that apply to the audit engagement, and to take appropriate action to eliminate threats to independence;
 - the need for the lead auditor to be satisfied that the audit team and any external experts collectively have the appropriate competence and capabilities;
 - the need for the lead auditor to take responsibility for the performance of the audit, specifically:
 - leading, supervising and carrying out the audit;

- ensuring that reviews are conducted in accordance with the SAI's review policies and procedures.

Engagement team management and skills

46. **The auditor should be satisfied that the entire audit team, and any external experts, collectively have the competence and capabilities to:**
- a) carry out the audit in accordance with the relevant standards and the applicable legal and regulatory requirements; and**
 - b) enable the auditor to issue a report that is appropriate in the circumstances.**
47. When addressing the competence and capabilities expected of the team as a whole, the auditor may consider the team's:
- Understanding, through appropriate training, and practical experience of audit engagements of a similar nature and complexity;
 - Understanding of professional standards and the applicable legal and regulatory requirements;
 - Technical expertise, including the relevant IT skills and knowledge of specialised areas of accounting or auditing;
 - Knowledge of relevant industries in which the audited organisation operates;
 - Ability to apply professional judgement;
 - Understanding of the SAI's quality control policies and procedures;
 - Ability to discharge the terms of the audit mandate in the relevant environment, including an understanding of the applicable reporting arrangements, and to report to the legislature or other governing body or in the public interest;
 - Skills in the field of performance auditing or compliance auditing, if relevant.

Principles related to basic audit concepts

48. ISSAIs 1000-2999 give best practice for the application of the Fundamental Principles of Financial Auditing. However, if an SAI chooses to develop standards based on the fundamental principles, or adopt national standards that are consistent with the principles, the matters covered by this and the following sections should be addressed.

Audit risk

49. **The auditor should reduce audit risk to an acceptably low level in the circumstances of the audit so as to obtain reasonable assurance as the basis for an opinion expressed in a positive form.**
50. The audit risk in an audit of financial statements is the risk that the auditor will express an inappropriate conclusion if the subject matter information is materially misstated. The auditor will reduce the risk to an acceptably low level in the circumstances of the audit to obtain reasonable assurance as the basis for expressing a conclusion in a positive form. To be meaningful, the level of assurance obtained by the auditor must enhance the intended users' confidence about the subject matter information to a degree that is clearly more than inconsequential.

51. In general, the audit risk depends on the following components:
- The risks of material misstatement consist of inherent risk and control risk:
 - a) Inherent risk – the susceptibility of the subject matter information to material misstatement, assuming that there are no related controls;
 - b) Control risk – the risk that a material misstatement could occur and will not be prevented, or detected and corrected, at the appropriate time by related controls. If relevant to the subject matter, some control risk will always exist because of the limitations inherent in the design and operation of internal controls.
 - Audit risk is a function of the risks of material misstatement and detection risk:
 - c) Detection risk – the risk that the auditor will not detect a material misstatement.
52. The assessment of risks is based on audit procedures to obtain information necessary for that purpose, as well as evidence obtained throughout the audit. The risk assessment is a matter of professional judgement and is not capable of precise measurement. The degree to which the auditor considers each element of risk will depend on the circumstances of the audit.

Professional judgement and professional scepticism

53. **The auditor should plan and perform the audit with professional scepticism, recognising that circumstances may exist that cause the financial statements to be materially misstated. When planning, performing, concluding and reporting an audit of financial statements, the auditor should exercise professional judgement.**
54. The terms “professional scepticism” and “professional judgement” are relevant when formulating requirements regarding the auditor's decisions about the appropriate response to matters concerning the audit. They express the attitude of the auditor, which includes a questioning mind. These concepts are set out in the ISSAIs on financial audit.
55. The concept of professional judgement is applied by the auditor at all stages of the audit process. It covers the application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, when making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement¹¹.
56. Professional judgement is necessary in particular in decisions about:
- materiality and audit risk;
 - the nature, timing and extent of the audit procedures used to meet the requirements of the ISSAIs and the ISAs and gather audit evidence;
 - evaluating whether sufficient appropriate audit evidence has been obtained, and whether more needs to be done to achieve the auditor's overall objectives;

¹¹ ISSAI 1200, paragraph 13.

- the evaluation of management's judgement in applying the financial reporting framework applicable to the audited entity;
- the drawing of conclusions from the audit evidence obtained – for example, assessing the reasonableness of the estimates made by management in preparing the financial statements.

57. Professional scepticism is fundamental to all audit engagements. The auditor plans and performs an assurance engagement with an attitude of professional scepticism, recognising that circumstances may exist that cause the subject matter information to be materially misstated. An attitude of professional scepticism means that the auditor makes a critical assessment, with a questioning mind, of the validity of the evidence obtained and is alert to evidence that contradicts or calls into question the reliability of documents or representations by the responsible party. Such an attitude is necessary throughout the audit process so as to reduce the risk of overlooking suspicious circumstances, over-generalising when drawing conclusions from observations, and using false assumptions to determine the nature, timing and extent of evidence-gathering procedures and evaluate the results thereof.

Materiality

58. **The auditor should apply the concept of materiality in an appropriate manner when planning and performing the audit.**

59. A misstatement is material, individually or when aggregated with other misstatements, if it could reasonably be expected to influence the decisions taken by users on the basis of the financial statements. Materiality has both quantitative and qualitative aspects. In the public sector, it is not limited to economic decisions by users, as decisions as to whether to continue certain government programmes or grant funding may be based on the financial statements. The qualitative aspects of materiality generally play a greater role in the public sector than in other types of entities. The assessment of materiality and the consideration of sensitivity and other qualitative factors in a particular audit are matters for the auditor's judgement.

60. When determining the audit strategy, the auditor should assess materiality for the financial statements as a whole. If, for one or more classes of transactions, account balances or disclosures, misstatements of amounts less than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users on the basis of the financial statements, the auditor should also determine the materiality level or levels to be applied to the classes of transactions, account balances or disclosures concerned.

61. The auditor should also determine performance materiality for the purposes of assessing the risk of material misstatement and determining the nature, timing and extent of further audit procedures. Planning the audit solely to detect individually material misstatements overlooks the fact that the aggregate of individually immaterial misstatements may cause the financial statements to be materially misstated, and leaves no margin for any undetected misstatements. Performance materiality should be set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements will exceed the materiality threshold for the financial statements as a whole. The determination of performance materiality involves the exercise of professional judgement. It is affected by the auditor's understanding of the entity, should be updated during the performance of risk assessment

procedures, and depends on the nature and extent of misstatements identified in previous audits and thus the auditor's expectations in terms of misstatements in the current period.

62. The concept of materiality is applied by the auditor in planning and performing the audit, as well as in evaluating the effect of identified misstatements on the audit and of any uncorrected misstatements, including omissions, on the financial statements. The auditor's opinion deals with the financial statements as a whole, and therefore the auditor is not responsible for detecting misstatements that are not globally material. The auditor should still identify and document quantitative immaterial misstatements, as they may be material due to their nature or when aggregated. Misstatements below the trivial threshold need not be considered.
63. The materiality determined when planning the audit does not necessarily establish an amount below which uncorrected misstatements, individually or in the aggregate, will always be evaluated as immaterial. The circumstances related to some misstatements may cause the auditor to evaluate them as material even if they are below materiality. Although it is not practicable to design audit procedures to detect misstatements that could be material solely because of their nature, the auditor considers not only the size but also the nature of uncorrected misstatements, and the particular circumstances of their occurrence, when evaluating their effect on the financial statements. The aspects the auditor considers include the sensitive nature of certain transactions or programmes, the public interest, the need for effective legislative oversight and regulation, and the nature of the misstatement or deviation (e.g. if it is a result of fraud or corruption).

Communication

64. **The auditor should identify the appropriate contact person(s) within the audited entity's governance structure and communicate with them regarding the planned scope and timing of the audit and any significant findings.**
65. The auditor should communicate with both management and those charged with governance. Communication entails obtaining information relevant to the audit and providing those charged with governance with timely observations that are significant and relevant to their oversight of the financial reporting process. It is important to promote effective two-way communication with those charged with governance.
66. In the public sector, identifying those charged with governance may be a challenge. The audited entity may be part of a larger or broader structure with governance bodies at several organisational levels and across different functions (i.e. vertically and horizontally). As a result, in some cases several distinct groups can be identified as being charged with governance. Furthermore, as an audit in the public sector might involve both financial statement objectives as well as compliance objectives, this too may involve separate governance bodies.
67. Communication should be in writing if the auditor determines that oral communication is not sufficient. The auditor may also be required to communicate with parties other than those within the organisation, such as the legislature, regulators or funding agencies.
68. Written communications need not include all matters arising during the course of the audit. However, written communication is vital for significant audit findings, which auditors are required to communicate to those charged with governance.

69. Auditors in the public sector are often the mandated auditors of the whole or major parts of the government and its administration. In this situation, auditors may have access to information from other audited entities and audits made in their regard, which might be of relevance to those charged with governance. Examples of this might include material errors in transactions with the audited entity that also affect other audited entities, or designs of relevant controls which have provided efficiency gains in other audited entities. Communicating this type of information to those charged with governance may add value to the audit when circumstances permit. However, laws, regulations or ethical requirements may prohibit communication of this type of information.

Documentation

70. **The auditor should prepare audit documentation that is sufficient to enable an experienced auditor, with no prior knowledge of the audit, to understand the nature, timing and extent of the audit procedures performed to comply with the relevant standards and the applicable legal and regulatory requirements, the results of those procedures and the audit evidence obtained, as well as significant matters arising during the audit, the conclusions reached in their regard, and significant professional judgments made in reaching those conclusions. The documentation should be prepared at the appropriate time.**
71. Adequate audit documentation is important for several reasons. It will:
- confirm and support the auditor's opinions and reports;
 - serve as a source of information for preparing reports or answering any enquiries from the audited organization or any other party;
 - serve as evidence of the auditor's compliance with the auditing standards;
 - facilitate planning, supervision and review;
 - help with the auditor's professional development;
 - help to ensure that delegated work has been satisfactorily executed; and
 - provide evidence of work done for future reference.
72. Auditing standards based on the fundamental principles need to include further requirements in relation to documentation in the following areas:
- the timely preparation of documentation;
 - the form, content and extent of documentation;
 - documentation requirements where the auditor judges it necessary to depart from a relevant requirement in the applied auditing standards;
 - documentation requirements where the auditor performs new or additional audit procedures or draws new conclusions after the date of the auditor's report;
 - the assembly of the final audit file.

The level 4 ISSAIs provide additional guidance on adopting requirements and audit documentation.

73. For auditors with a judicial role, such as a court of accounts, documentation forms part of the basis of official rulings. In this environment, due process of law may establish specific and strict requirements to be adhered to regarding confidentiality of documentation in connection with the proceedings of a case. Additionally, as decisions may result in a legally binding public credit, public-sector auditors may be subject to supplementary documentation retention requirements.

Principles related to the audit process

Agreeing the terms of the engagement

74. **The auditor should agree or, if the terms of the engagement are clearly mandated, establish a common understanding of the terms of the audit engagement with management or those charged with governance.**
75. The terms of an audit engagement in the public sector are normally mandated and therefore not subject to requests from, and agreement with, management or those charged with governance. Instead of agreeing the terms formally, public-sector auditors may instead choose to establish a common formal understanding of the respective roles and responsibilities of the management and the auditor. Since the public-sector auditor is normally engaged by and reports to the legislature, agreements may need to be reached with both the legislature and those charged with governance.
76. The auditor should communicate to the appropriate representatives of those charged with governance the auditor's responsibilities with regard to the audit of financial statements, including the auditor's responsibility to form and express an opinion on the financial statements prepared by management under the oversight of those charged with governance.
77. If the terms of the engagement are prescribed in sufficient detail by law or regulation, it may not be necessary to record them in an audit engagement letter or other suitable form of written agreement. One exception may be the statement by management and, where appropriate, those charged with governance, that they acknowledge and understand the responsibilities set out in the specific auditing standards, such as the ISSAIs and the ISAs. As such engagements are common in the public sector, written agreements on the terms need not be concluded, although they may assist in clarifying the responsibilities of the parties involved.
78. Those charged with governance should also be sent an overview of the planned scope and timing of the audit. The auditor should include views about significant qualitative aspects of the audited entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures.
79. SAIs are normally required to carry out audits as mandated. They do not normally have the option of rejecting an assignment, even if the preconditions are not met. Standards developed on the basis of the fundamental principles must provide guidance on suitable action in such circumstances. ISSAI 1210¹² includes guidance in this regard.

¹² ISSAI 1210 – Agreeing the Terms of an Engagement.

Planning

80. The auditor should develop an overall audit strategy that includes the scope, timing and direction of the audit, as well as an audit plan.

81. An overall audit strategy will guide the auditor in the development of the audit plan. When developing the audit strategy, the auditor needs to:

- identify the characteristics of the engagement that define its scope;
- ascertain the reporting objectives of the engagement so as to plan the timing of the audit and the nature of the communications required;
- consider the factors that, in the auditor's professional judgement, are significant in directing the engagement team's efforts;
- consider the results of preliminary activities and, where applicable, whether knowledge gained on other engagements performed by the auditor engaged for the audited entity is relevant;
- ascertain the nature, timing and extent of resources necessary to carry out the engagement;
- consider the results and knowledge obtained from performance audits and other audit activities relevant to the audited entity, including the implications of previous recommendations;
- consider and assess the expectations of the legislature and other relevant users of the audit report.

82. The auditor should plan the audit properly to ensure that it is conducted in an effective and efficient manner.

83. The auditor should prepare an audit plan, which should include a description of:

- the nature, timing and extent of planned risk assessment procedures;
- the nature, timing and extent of planned further audit procedures at the assertion level;
- other planned audit procedures that are necessary so that the engagement complies with the applicable standards. Such procedures may include or describe: a review of the legal framework for the audit; a brief description of the activity, programme or entity to be audited; the reasons for carrying out the audit; the factors affecting the audit, including those determining the materiality of matters to be considered; the audit objectives and scope; the audit approach; the characteristics of the audit evidence to be collected, and the procedures required to collect and analyse evidence; the necessary resources; a timetable for the audit; the form, content and users of the auditor's report and management letter.

84. Both the overall strategy and the audit plan need to be documented. They must also be updated, as necessary, during the course of the audit.

Understanding the audited entity

85. The auditor should have an understanding of the audited entity and its environment, including internal control procedures that are relevant to the audit.

86. Understanding the different aspects of the organisation and its environment enables the auditor to effectively plan and perform the audit. The necessary understanding will include:

- the relevant environment, regulations and other external factors, including the applicable financial reporting framework;
 - the nature of the audited entity, including its mode of operation, governance structure, funding (to enable the auditor to understand the classes of transactions, account balances and disclosures to be expected in the financial statements), and the selection and application of accounting policies, including the reasons for changes thereto;
 - measurement and review of the audited entity's financial performance;
 - decisions initiated outside the audited entity as a result of political processes such as new programmes or budget constraints;
 - specific laws and regulations to which the audited entity is subject, and the potential impact of non-compliance with these;
 - programme objectives and strategies, which may include public policy elements and therefore have implications for the risk assessment;
 - governance structures affected by the legal structure of the audited entity, for example whether the entity is a ministry, department, agency or other type of public-sector body.
87. To obtain an understanding of the control environment, it may be relevant to consider the audited entity's communication and enforcement of integrity and ethical values, its commitment to competence, participation by those charged with governance, the management's philosophy and operating style, organisational structure, the existence and level of internal audit activity, the assignment of authority and responsibility, and human resource policies and practices.
88. Relevant audit evidence may be obtained through a combination of inquiries and other risk assessment procedures, such as the corroboration of inquiries through observation or inspection of documents. For example, by interviewing management and employees, the auditor may obtain an understanding of how management shares with staff its views on business practices and ethical behaviour. The auditor may then determine whether relevant controls have been implemented by considering, for example, whether management has a written code of conduct and whether it acts in accordance with the code.
89. As part of the understanding process, the auditor also needs to consider whether the audited entity has a procedure for identifying business risks relevant to financial reporting objectives, and whether it further estimates the significance of those risks by assessing the likelihood of their occurrence. If such a procedure has been established, the auditor needs to obtain an understanding of it, and the results thereof.
90. The auditor's understanding of internal control relevant to financial reporting may include the following areas:
- the classes of transactions in the audited entity's operations that are significant to the financial statements;
 - the procedures, both manual and using IT, by which those transactions are initiated, recorded, processed, corrected as necessary, transferred to the general ledger and reported in the financial statements;
 - the accounting records, supporting information and specific accounts in the financial statements that are used to initiate, record, process and report transactions; this includes procedures for correcting incorrect information and transferring information to the general ledger;

- how the information system captures events and conditions, other than transactions, that are significant to the financial statements;
- the financial reporting process used to prepare the audited entity's financial statements, including significant accounting estimates and disclosures;
- controls surrounding journal entries, including non-standard journal entries used to record unusual non-recurring transactions or adjustments;
- relevant controls that relate to compliance with authorities;
- controls related to monitoring performance against the budget;
- controls related to transferring budgetary funds to other audited entities;
- controls of classified national security and sensitive personal data, such as tax and health information; and
- supervision and other controls performed by parties outside the audited entity in areas such as:
 - compliance with laws and regulations, such as procurement regulations;
 - execution of the budget;
 - other areas as defined by legislation or audit mandate; and
 - management accountability.

91. Auditing does not require an understanding of all the controls carried out for each significant class of transactions, account balance and disclosure in the financial statements, or for every assertion relevant to them. However, an understanding of an audited entity's controls and, if relevant, government-wide controls is not sufficient to test their operating effectiveness unless a degree of automation provides for consistency in the implementation of the controls.

Risk assessment

92. **The auditor should assess the risks of material misstatement at the financial statement level and the assertion level for classes of transactions, account balances and disclosures so as to provide a basis for further audit procedures.**

93. Risk assessment procedures may include:

- inquiries of management and staff within the audited entity who, in the auditor's judgement, may have information that could assist in identifying risks of material misstatement due to fraud or error;
- analytical procedures;
- observation and inspection.

94. The risks of material misstatement should be identified and assessed at both the financial statement level and the assertion level for classes of transactions, account balances and disclosures so as to provide a basis for designing and performing further audit procedures. For this purpose, the auditor needs to:

- identify risks throughout the process of obtaining an understanding of the audited entity and its environment, by examining relevant controls that relate to the risks and considering the classes of transactions, account balances and disclosures in the financial statements;
- assess the risks identified and evaluate whether they relate more pervasively to the financial statements as a whole and could potentially affect many assertions;

- relate the risks identified to what could go wrong at the assertion level, taking account of relevant controls that the auditor intends to test; and
 - consider the likelihood of misstatement, including the possibility of multiple misstatements, and whether the potential for misstatement is such as to render it material.
95. As part of the risk assessment, the auditor determines whether any of the risks identified are, in the auditor's judgment, significant. In exercising this judgement, the auditor should exclude the effects of controls identified in relation to the risk. When judging which risks are significant, the auditor needs to consider at least the following:
- whether the risk is a risk of fraud;
 - whether the risk is related to recent significant economic, accounting or other developments and, therefore, requires specific attention;
 - the complexity of transactions;
 - whether the risk involves significant transactions with related parties;
 - the degree of subjectivity in the measurement of financial information related to the risk, especially measurements which involve a wide range of measurement uncertainty;
 - whether the risk involves significant transactions that are outside the audited entity's normal course of business, or that otherwise appear to be unusual; and
 - whether the risk also affects compliance with laws and regulations.
96. The identification and assessment of the risks of material misstatement at both the financial statement level and assertion level, and the related controls about which the auditor has obtained understanding, must be sufficiently documented.

Responses to assessed risks

97. **The auditor should act appropriately to address the assessed risks of material misstatement in the financial statements.**
98. Responses to assessed risks include designing audit procedures that address the risks, such as substantive procedures and test of controls. Substantive procedures include both tests of details and substantive analysis of classes of transactions, account balances and disclosures.
99. The nature, timing and extent of audit procedures are based on and are responsive to the assessed risks of material misstatement at the assertion level. In designing the necessary audit procedures, the auditor should consider the reasons for the assessed risks of material misstatement at the assertion level for each class of transactions, account balance and disclosure. Such reasons may include the inherent risk of transactions (the likelihood of material misstatement due to the particular characteristics of the relevant class of transactions, account balance or disclosure) and the control risk (whether the risk assessment takes account of relevant controls).
100. Examination of the control risk requires the auditor to obtain evidence that the controls are operating effectively (that is, the auditor intends to rely on the operating effectiveness of controls when determining the nature, timing and extent of substantive procedures).

101. When designing and performing tests of the relevant controls to obtain sufficient appropriate evidence as to their operating effectiveness, the auditor should consider that, the greater the reliance placed on the effectiveness of a control, the more persuasive should be the audit evidence obtained.
102. **The auditor should design and perform substantive procedures for each material class of transactions, account balance and disclosure, irrespective of the assessed risks of material misstatement.**
103. The auditor should always undertake some substantive testing, irrespective of whether controls have been tested. In addition, if the auditor has determined that an assessed risk of material misstatement at the assertion level is significant, substantive procedures should be performed that specifically respond to that risk. When the approach to a significant risk consists only of substantive procedures, those procedures should include tests of details.

Considerations relating to fraud in an audit of financial statements

104. **The auditor should identify and assess the risks of material misstatement in the financial statements due to fraud, should obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud and should respond appropriately to fraud or suspected fraud identified during the audit.**
105. The primary responsibility for the prevention and detection of fraud rests with the entity's management and those charged with governance. It is important that management, under the oversight of those charged with governance, strongly emphasise fraud prevention (limiting opportunities for fraud to take place) and fraud deterrence (dissuading individuals from committing fraud because of the likelihood of detection). The auditor is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error.
106. Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor is whether the action resulting in a misstatement was intentional or unintentional. Although fraud is a broad legal concept, the auditor is concerned only with fraud that causes a material misstatement in the financial statements. Two types of intentional misstatements are relevant to the auditor – misstatements resulting from fraudulent financial reporting and those resulting from the misappropriation of assets.
107. The auditor is expected to maintain an attitude of professional scepticism throughout the audit, recognising the possibility of material misstatement due to fraud at both the financial statement level and the assertion level for classes of transactions, account balances and disclosures, notwithstanding the auditor's past experience of the honesty and integrity of the management and those charged with governance. When performing risk assessment procedures and related activities to obtain an understanding of the audited entity and its environment, the auditor should seek to obtain information that can be used to identify risks of material misstatement due to fraud.

108. Areas in which auditors should be alert to fraud risks leading to material misstatement may include procurement, grants, privatisations, intentional misrepresentation of results or information and misuse of authority or power. When developing standards based on these fundamental principles, the guidance on fraud risk areas in ISSAI 1240 may be of assistance.
109. Requirements for the reporting of fraud in the public sector may be the subject of specific provisions in the audit mandate or related laws or regulations, and the auditor may be required to communicate such issues to parties outside the audited entity, such as regulatory and enforcement authorities. In some environments, there may be a specific obligation to refer indications of fraud to investigative bodies and even to cooperate with such bodies on determining whether fraud or abuse has occurred. In other environments, auditors may be obliged to report circumstances that may indicate the possibility of fraud or abuse to the competent jurisdictional body or to the appropriate part of the government or legislature, such as prosecutors, the police or (if relevant to legislation) affected third parties. Auditors should also consider that the use of public monies tends to raise the profile of fraud. As a result auditors may need to be responsive to public expectations regarding fraud detection. ISSAI 1240 makes reference to the possibility of extending reporting responsibilities within the public sector so as to address concerns about public accountability.

Going-concern considerations

110. **The auditor should consider whether there are events or conditions that may cast significant doubt on the audited entity's ability to continue as a going concern.**
111. Financial statements are normally prepared on the assumption that the audited entity is a going concern and will continue to meet its statutory obligations for the foreseeable future. In assessing whether the going-concern assumption is appropriate, those responsible for preparation of the financial statements take into account all available information for the foreseeable future. General-purpose financial statements are prepared on a going-concern basis unless the legislature has decided to liquidate the audited entity or that it should cease operation.
112. The going-concern concept may have little or no relevance for “ordinary” public-sector entities such as those funded through appropriations on the government budget. When such organisations are abolished or merged with others, their liabilities and assets are usually taken over by other public-sector entities. For some types of entities, such as government business enterprises and joint ventures with other principals (including private sector entities operating in legal forms that provide for limited owner liability), this may not be the case. The responsibility for implementing government programmes may also be contracted out to private sector organisations, such as NGOs and private companies, but the programmes may still be audited by the SAI. There is a general trend towards outsourcing, making the going-concern concept and the auditor's judgement in this regard increasingly relevant to public-sector audit.
113. Some financial reporting frameworks contain an explicit requirement for management to make a specific assessment of the audited entity's ability to continue as a going concern, as well as standards relating to the matters to be considered and disclosures to be made in this regard. Since the going-concern assumption is a fundamental principle in the preparation of financial statements, management must assess the audited entity's ability to continue as a going concern even if the financial reporting framework does not explicitly require them to do so.

114. The auditor should obtain sufficient appropriate audit evidence about the suitability of management's use of the going-concern assumption in the preparation and presentation of financial statements, and should conclude as to whether there is any material uncertainty about the audited entity's ability to continue as a going concern. If the financial statements were prepared on a going-concern basis but, in the auditor's judgement, the use of the going-concern assumption is inappropriate, the auditor should express an adverse opinion. If the auditor concludes that use of the going-concern assumption is appropriate in the circumstances and adequate disclosure is made in the financial statements, but that a material uncertainty exists, the auditor should express an unmodified opinion and include an Emphasis of Matter paragraph. If such disclosure is not made in the financial statements, the auditor should express a qualified or adverse opinion, as appropriate, in accordance with ISSAI 1705¹³.
115. The degree of consideration will depend on the facts in each case, and assessments of the going-concern assumption are not predicated on the solvency test usually applied to business enterprises. In certain circumstances, while the usual going-concern tests of liquidity and solvency may appear unfavourable, other factors may suggest that the audited entity is nonetheless a going concern. For example:
- In assessing whether a government is a going concern, the power to levy rates or taxes may enable some audited entities to be considered as going concerns even though they may operate for extended periods with negative net assets/equity; and
 - Assessment of an individual audited entity's statement of financial position at the reporting date may suggest that use of the going-concern assumption in the preparation of its financial statements is not appropriate. However, there may be multi-year funding agreements or other arrangements in place that will ensure the continued operation of the audited entity.
116. Generally speaking, determining whether the going-concern assumption is appropriate is relevant to individual audited entities rather than to government as a whole. In the case of individual audited entities, before concluding that use of the going-concern assumption is appropriate, those responsible for the preparation of financial statements may need to consider a wide range of factors surrounding current and expected performance, the potential or announced restructuring of organisational units, revenue estimates or the likelihood of continued government funding, and potential sources of replacement financing.
117. When performing risk assessment procedures the auditor should consider whether there are any events or conditions that may cast significant doubt on the audited entity's ability to continue as a going concern. In forming a view of the audited entity's ability to continue its operations, the auditor should examine two separate but sometimes overlapping factors:
- the greater risk associated with changes in policy direction (for example, where there is a change in government); and
 - the less common operational, or business, risk (for example, where an audited entity has insufficient working capital to continue its operations at the existing level).

¹³ ISSAI 1705 – Modifications to the Opinion in the Independent Auditor's Report.

Considerations relating to laws and regulations in an audit of financial statements

118. **The auditor should identify the risks of material misstatement due to direct and material non-compliance with laws and regulations. Identification of such risks should be based on a general understanding of the legal and regulatory framework applicable to the specific environment in which the audited entity operates, including how the audited entity complies with that framework.**

The auditor should obtain sufficient appropriate audit evidence regarding compliance with the laws and regulations that are generally recognised to have a direct and material effect on the determination of material amounts and disclosures in financial statements.

119. The auditor is expected to obtain reasonable assurance as to whether the financial statements, taken as a whole, are free from material misstatement, whether due to fraud or error. However, the auditor is not responsible for preventing non-compliance and cannot be expected to detect all breaches of laws and regulations.
120. When conducting an audit of financial statements in accordance with standards based on or consistent with ISSAI 200, the auditor needs to have an understanding of the legal and regulatory framework applicable to the entity.
121. The effect of laws and regulations on the financial statements varies considerably. The laws and regulations to which an audited entity is subject constitute the applicable legal and regulatory framework. The provisions of some laws or regulations have a direct effect on the financial statements in that they determine the nature of reported amounts and disclosures. While other laws or regulations are to be complied with by management or set the terms under which the audited entity is allowed to conduct its operations, they do not have a direct effect on the entity's financial statements.
122. Non-compliance with laws and regulations may result in fines, litigation or other consequences for the audited entity that may have a material effect on the financial statements.
123. In the public sector, the distribution by an agency of grants and subsidies may be subject to specific laws and regulations that will have a direct impact on the financial statements. Often the financial reporting framework may also include information such as a budget report, appropriation report or performance report. Where the financial reporting framework includes such information, the auditor may need to consider specific laws and regulations that could affect it directly or indirectly.
124. Matters involving non-compliance with laws and regulations that come to the auditor's attention during the course of the audit should be communicated to those charged with governance, save where the matters are clearly inconsequential. However, the audit mandate, or obligations for public-sector entities arising from legislation, regulation, ministerial directives, government policy requirements or resolutions by the legislature, may result in additional objectives, such as the responsibility to report all instances of non-compliance with authorities, even where clearly inconsequential.

125. This broader scope of reporting may, for example, include the obligation to express a separate opinion as to the audited entity's compliance with laws and regulations, or to report cases of non-compliance. These additional objectives are dealt with in *ISSAI 400 – Fundamental Principles of Compliance Auditing* and the related guidelines¹⁴. However, even where there are no such additional objectives, there may be general public expectations in regard to the auditors' reporting of non-compliance with authorities. The auditors should therefore bear such expectations in mind and be alert to instances of non-compliance.

Audit evidence

126. The auditor should perform audit procedures in such a way as to obtain sufficient appropriate audit evidence and thus draw conclusions on which to base the auditor's opinion.

127. Audit procedures should be appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence. Audit evidence comprises information contained in the accounting records underlying the financial statements and from other sources. The auditor should consider both the relevance and the reliability of the information to be used as audit evidence. An audit of financial statements does not involve the authentication of documentation, nor is the auditor trained as or expected to be an expert in such authentication. However, the auditor should consider the reliability of the information to be used as evidence, including photocopies, facsimiles, filmed, digitised or other electronic documents, and take account, where relevant, of controls over their preparation and maintenance.

128. Audit evidence should be sufficient and appropriate. Sufficiency is a measure of the quantity of evidence, while appropriateness relates to the quality of evidence – its relevance and reliability. The quantity of evidence required depends on the risk of material misstatement of the subject matter information (the greater the risk, the more evidence is likely to be required) and on the quality of such evidence (the higher the quality, the less may be required). Accordingly, the sufficiency and appropriateness of evidence are interrelated. However, merely obtaining more evidence does not compensate for its poor quality.

129. The reliability of evidence is influenced by its source and nature, and is dependent on the specific circumstances in which the evidence was obtained. Generalisations about the reliability of various kinds of evidence can be made – but with important exceptions. Even when evidence was obtained from sources external to the audited entity, such as external confirmations, circumstances may exist that could affect the reliability of the information. While recognising that exceptions may exist, the following generalisations about the reliability of evidence may be useful:

- Evidence is more reliable when it is obtained from independent sources outside the audited entity.
- Evidence that is generated internally is more reliable when the related controls are effective.

¹⁴ ISSAI 4000 – Compliance Audit Guidelines – General Introduction and ISSAI 4200 – Compliance Audit Guidelines Related to the Audit of Financial Statements.

- Evidence obtained directly by the auditor (for example, through observation of the application of a control) is more reliable than evidence obtained indirectly or by inference (for example, through inquiry into the application of a control).
- Evidence is more reliable when it exists in documentary form, whether paper, electronic, or other media (for example, a simultaneous written record of a meeting is more reliable than a subsequent oral report of what was discussed).
- Evidence provided by original documents is more reliable than evidence provided by photocopies or facsimiles.

130. Greater assurance is ordinarily provided by consistent evidence obtained from different sources, or of a different nature, than by items of evidence considered individually. In addition, by obtaining evidence from different sources or of a different nature, it may be possible to identify individual items of evidence that are unreliable.

131. Audit evidence may be obtained by testing accounting records. As well as information that supports and corroborates management assertions, account should be taken of any information that contradicts those assertions. In the case of financial statements in the public sector, management may often assert that transactions and events were carried out in accordance with the legislation or due authority, and such assertions may well lie within the scope of a financial audit. It may also be necessary for auditors in the public sector to consider the requirements and guidance in the Fundamental Principles of Compliance Auditing and the related guidelines¹⁵ when developing or adopting standards in such cases.

132. When adopting or developing auditing standards, SAIs should also consider the need for requirements to obtain sufficient and appropriate audit evidence in relation to:

- the use of external confirmations as audit evidence;
- audit evidence from analytical procedures and different audit sampling techniques;
- audit evidence from the use of fair value measurement, if relevant;
- audit evidence when the audited entity has related parties;
- audit evidence from the audited entity's use of service organisations;
- audit evidence from using the work of internal audit functions or, when allowed by law or regulation and considered relevant, the direct assistance of internal auditors;
- audit evidence from external experts;
- the use of written representations to support audit evidence.

Further guidance on such procedures and requirements are included in the level 4 ISSAIs, which may be of assistance for SAIs when developing further requirements in these areas.

133. Auditors in certain environments, such as a court of accounts, may be subject to laws and regulations requiring them to understand and follow precise procedures related to rules of evidence. Public-sector auditors should familiarise themselves with any such policies and procedures that describe additional requirements relating to audit evidence and are designed to ensure compliance with the applicable rules.

¹⁵ ISSAIs 400, 4000 and 4200.

Consideration of subsequent events

134. **The auditor should obtain sufficient appropriate audit evidence that all events occurring between the date of the financial statements and the date of the auditor’s report that require an adjustment to, or disclosure in, the financial statements have been identified. The auditor should also respond appropriately to facts that became known after the date of the auditor’s report and which, had they been known at that date, might have caused the auditor to amend the auditor’s report.**
135. Procedures should be designed, as nearly as possible, to cover the period from the date of the financial statements to the date of the auditor’s report. The auditor is not, however, expected to perform additional audit procedures on matters to which previous audit procedures have provided satisfactory conclusions. Financial statements may be affected by certain types of subsequent events (those occurring after the date of the financial statements). Many financial reporting frameworks specifically refer to such events. Ordinarily, two types of event are identified:
- a) Events that provide evidence of conditions that existed at the date of the financial statements; and
 - b) Events that provide evidence of conditions that arose after the date of the financial statements.
136. Procedures for obtaining sufficient appropriate audit evidence may include:
- steps to obtain an understanding of any procedures established by management to ensure that subsequent events are identified;
 - inquiries of management;
 - scrutiny of minutes;
 - scrutiny of the entity’s most recent interim financial statements, if any.

When making inquiries of management, auditors may need to consider subsequent events that are relevant to the government entity’s ability to fulfil its programme objectives and may therefore affect the presentation of performance information in the financial statements.

137. The auditor is under no obligation to perform any audit procedures on the financial statements after the date of the auditor’s report. However, if, after the date of the auditor’s report but before the financial statements have been issued, a fact becomes known to the auditor that, had it been known at the date of the auditor’s report, might have caused an amendment to the report, appropriate action should be taken. Such action may include:
- discussing the matter with the management and, where appropriate, those charged with governance,
 - determining whether the financial statements need amendment and, if so,
 - inquiring how the management intends to address the matter in the financial statements.

138. If the management does not take the necessary steps to ensure that anyone in receipt of the financial statements, where already issued, is informed of the situation, and does not amend the financial statements in circumstances where the auditor believes they need to be amended, the auditor should notify the management and those charged with governance that the auditor will seek to prevent future reliance on the auditor's report. This may entail seeking legal advice and reporting to the appropriate statutory body. Further guidance is included in ISSAI 1560¹⁶.

Evaluating misstatements

139. **The auditor should keep a full record of misstatements identified during the audit, and communicate to management and those charged with governance, as appropriate and on a timely basis, all misstatements recorded during the course of the audit.**
140. Uncorrected misstatements should be evaluated for materiality, individually or in aggregate, to determine what effect they may have on the opinion to be given in the auditor's report.
141. The auditor should invite the management to correct misstatements, and if the management refuses to correct some or all communicated misstatements the auditor should find out why. When evaluating whether the financial statements as a whole are misstated, the auditor should consider the reasons given for not making corrections. Those charged with governance should be notified of uncorrected misstatements and the effect that they may have, individually or in aggregate, on the opinion in the auditor's report. The auditor's notification should individually identify uncorrected material misstatements in classes of transactions, account balances or disclosures.
142. Misstatements that are clearly trivial need not normally be communicated, save where the auditor is required by mandate to report all misstatements. The auditor needs to determine whether uncorrected misstatements are material, individually or in the aggregate. To this end, the auditor should consider;
- the size and nature of the misstatements, in relation both to particular classes of transactions, account balances or disclosures and to the financial statements as a whole, and the particular circumstances of their occurrence; and
 - the effect of uncorrected misstatements from prior periods on the relevant classes of transactions, account balances or disclosures, and on the financial statements as a whole.

Further guidance on evaluating misstatements is included in ISSAI 1450¹⁷.

¹⁶ ISSAI 1560 – Subsequent Events.

¹⁷ ISSAI 1450 – Evaluation of Misstatements Identified during the Audit.

Forming an opinion and reporting on the financial statements

143. **The auditor should form an opinion based on an evaluation of the conclusions drawn from the audit evidence obtained, as to whether the financial statements as a whole are prepared in accordance with the applicable financial reporting framework. The opinion should be expressed clearly in a written report that also describes the basis for the opinion.**
144. The objectives of a financial audit in the public sector are often broader than expressing an opinion as to whether the financial statements have been prepared, in all material respects, in accordance with the applicable financial reporting framework. The audit mandate, or legislation, regulation, ministerial directive, government policy requirements or resolutions by the legislature, may include additional objectives of equal importance to the opinion on the financial statements. These additional objectives may include audit and reporting responsibilities relating, for example, to any findings of non-compliance with authorities. However, even where no additional objectives are set, there may be general public expectations in regard to the reporting of non-compliance with authorities or the effectiveness of internal controls.
145. Auditors with responsibilities relating to reporting on compliance or non-compliance with authorities may consider the Fundamental Principles of Compliance Auditing and related guidelines¹⁸.
146. In order to form an opinion, the auditor must first conclude whether reasonable assurance has been obtained as to whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. The conclusion should take into account:
- a) Whether sufficient appropriate evidence has been obtained;
 - b) Whether uncorrected misstatements are material, individually or in aggregate; and
 - c) The auditor's evaluations of the following points, which are taken into consideration when determining the form of the opinion:
 - Whether the financial statements are prepared in all material respects, in accordance with requirements of the applicable financial reporting framework, including consideration of the qualitative aspects of the entity's accounting practices, such as possible bias in management's judgments.
 - Whether the financial statements adequately disclose the significant accounting policies selected and applied,
 - Whether the accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate,
 - Whether the accounting estimates made by management are reasonable,
 - Whether the information presented in the financial statements is relevant, reliable, comparable, and understandable,

¹⁸ ISSAIs 400, 4000 and 4200.

- Whether the financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements,
- Whether the terminology used in the financial statements, including the title of each financial statement, is appropriate,
- Whether the financial statements adequately refer to or describe the applicable financial reporting framework.

d) Where the financial statements have been prepared in accordance with a fair presentation framework, the conclusion should also consider whether the financial statements achieve fair presentation:

- in terms of overall presentation, structure and content;
- whether the financial statements, including the related notes, fairly present the underlying transactions and events.

Form of opinion

147. The auditor should express an unmodified opinion if it is concluded that the financial statements are prepared, in all material respects, in accordance with the applicable financial framework.

If the auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, or is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement, the auditor should modify the opinion in the auditor's report in accordance with the section on "Determining the type of modification to the auditor's opinion".

148. If financial statements prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation, the auditor should discuss the matter with the management and, depending on the requirements of the applicable financial reporting framework and how the matter is resolved, determine whether it is necessary to modify the audit opinion.

Elements required in the auditor's report

149. The auditor's report should be in written form and contain the following elements:

- A title that clearly indicates that it is the report of an independent auditor.
- An addressee as required by the circumstances of the engagement.
- An introductory paragraph that (1) identifies whose financial statements have been audited, (2) states that the financial statements have been audited, (3) identifies the title of each statement comprising the financial statements, (4) refers to the summary of significant accounting policies and other explanatory information, and (5) specifies the date or period covered by each financial statement comprising the financial statements.
- A section with the heading "Management's responsibility for the financial statements", stating that the management is responsible for the financial statements in accordance with the applicable financial reporting framework and for internal controls to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

- A section with the heading “Auditor’s responsibility”, stating that the responsibility of the auditor is to express an opinion based on the audit of the financial statements, and describing an audit as involving procedures to obtain audit evidence about the amounts and disclosures in the financial statements, the procedures selected being dependent on the auditor’s judgement as to, *inter alia*, the risks of material misstatement of the financial statements, whether due to fraud or error. In making the risk assessment, the auditor should consider internal controls relevant to the entity’s preparation of the financial statements and design audit procedures that are appropriate in the circumstances. This section should also refer to the evaluation of the appropriateness of the accounting policies used and the reasonableness of the accounting estimates made by the management, as well as the overall presentation of the financial statements. It should be stated whether the auditor believes that the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor’s opinion.
- A section with the heading “Opinion” which should use one of the following equivalent phrases when expressing an unmodified opinion on the financial statements prepared in accordance with a fair presentation framework:
 - *The financial statements present fairly, in all material respects,... in accordance with [the applicable reporting framework];* or
 - *The financial statements give a true and fair view of ... in accordance with [the applicable financial reporting framework].*

When expressing an unmodified opinion on financial statements prepared in accordance with a compliance framework, the auditor’s opinion should be that the financial statements are prepared, in all material respects, in accordance with [the applicable financial reporting framework].

If the reference to the applicable financial reporting framework is not to the IPSASs or the IFRSs, the auditor’s opinion should identify the jurisdiction of origin of the framework.

- If required, or as determined by the auditor, a section with the heading “Report on other legal and regulatory requirements” or otherwise as appropriate to the content of the section, addressing other reporting responsibilities in the auditor’s report on the financial statements that are in addition to the requirement to report on the financial statements.
- The auditor’s signature.
- The date on which the auditor obtained sufficient appropriate evidence on which to base the auditor’s opinion on the financial statements, including evidence that:
 - all the statements comprising the financial statements, including the related notes, have been prepared; and
 - those with the recognised authority have asserted that they take responsibility for the financial statements.
- The location in the jurisdiction where the auditor practises.

150. In addition to the opinion, the auditor may be required by law or regulation to report observations and findings which have not affected the opinion and any recommendations made as a result thereof. These elements should be clearly separate from the opinion.

Modifications to the opinion in the auditor's report

151. The auditor should modify the opinion in the auditor's report if it is concluded that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, or if the auditor was unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement. Auditors may issue three types of modified opinions: a qualified opinion, an adverse opinion and a disclaimer of opinion.

Determining the type of modification to the auditor's opinion

152. The decision regarding which type of modified opinion is appropriate depends upon:

- The nature of the matter giving rise to the modification – that is, whether the financial statements are materially misstated or, in the event that it was impossible to obtain sufficient appropriate audit evidence, may be materially misstated; and
- The auditor's judgment about the pervasiveness of the effects or possible effects of the matter on the financial statements.

153. The auditor should express a qualified opinion if: (1) having obtained sufficient appropriate audit evidence, the auditor concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or (2) the auditor was unable to obtain sufficient appropriate audit evidence on which to base an opinion, but concludes that the effects on the financial statements of any undetected misstatements could be material but not pervasive.

154. The auditor should express an adverse opinion if, having obtained sufficient appropriate audit evidence, the auditor concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

155. The auditor should disclaim an opinion if, having been unable to obtain sufficient appropriate audit evidence on which to base the opinion, the auditor concludes that the effects on the financial statements of any undetected misstatements could be both material and pervasive. If, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the audit scope that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor should request that management remove the limitation.

156. If expressing a modified audit opinion, the auditor should also modify the heading to correspond with the type of opinion expressed. ISSAI 1705¹⁹ provides additional guidance on the specific language to use when expressing a modified opinion and describing the auditor's responsibility. It also includes illustrative examples of reports.

¹⁹ ISSAI 1705 – Modifications to the Opinion in the Independent Auditor's Report.

Emphasis of Matter paragraphs and Other Matters paragraphs in the auditor's report

157. If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that is of such importance that it is fundamental to their understanding of the financial statements, but there is sufficient appropriate evidence that the matter is not materially misstated in the financial statements, the auditor should include an Emphasis of Matter paragraph in the auditor's report. Emphasis of Matter paragraphs should only refer to information presented or disclosed in the financial statements.

158. An Emphasis of Matter paragraph should:

- be included immediately after the opinion;
- use the Heading "Emphasis of Matter" or another appropriate heading;
- include a clear reference to the matter being emphasised and indicate where the relevant disclosures that fully describe the matter can be found in the financial statements; and
- indicate that the auditor's opinion is not modified in respect of the matter emphasised.

159. If the auditor considers it necessary to communicate a matter, other than those that are presented or disclosed in the financial statements, which, in the auditor's judgement, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report, and provided this is not prohibited by law or regulation, this should be done in a paragraph with the heading "Other Matter," or another appropriate heading. This paragraph should appear immediately after the opinion and any Emphasis of Matter paragraph.

160. If the auditor expects to include either or both of these paragraphs in the auditor's report, the auditor should communicate that expectation and the wording of such paragraphs to those charged with governance. The auditor may also be required or decide to notify other parties, such as the legislature, in addition to those charged with governance.

161. Public-sector audit mandates or expectations may expand the circumstances in which it would be relevant to include an Emphasis of Matter paragraph (concerning a matter properly disclosed in the financial statements) or an Other Matters paragraph (concerning information not disclosed in the financial statements).

Comparative information – corresponding figures and comparative financial statements

162. Comparative information¹ refers to amounts and disclosures included in the financial statements in respect of one or more prior periods. The auditor should determine whether the financial statements include the comparative information required by the applicable financial reporting framework, and whether such information is correctly classified. To accomplish this, the auditor should evaluate whether:

- the comparative information agrees with the amounts and other disclosures that were presented in the prior period or, where appropriate, have been restated; and
- the accounting policies reflected in the comparative information are consistent with those applied in the current period or, if there have been changes in accounting policies, whether those changes have been properly accounted for and adequately presented and disclosed.

163. If the auditor becomes aware, during the current period, of a possible material misstatement in the comparative information, the auditor should perform such additional audit procedures as are necessary in the circumstances to obtain sufficient appropriate audit evidence as to whether a material misstatement exists.
164. Comparative information may take the form of corresponding figures which are included as an integral part of the current period financial statements and are intended to be read only in relation to the amounts and other disclosures relating to the current period. When corresponding figures are presented, the auditor's opinion should not refer to them save in the following circumstances:
- If the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion or an adverse opinion, and if the matter which gave rise to the modification is unresolved, the auditor should express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements, modified with respect to the corresponding figures included therein.
 - If the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements on which an unmodified opinion was issued, and if the corresponding figures have not been properly restated or appropriate disclosures have not been made, the auditor should express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements.
 - If the prior period financial statements were not audited, the auditor should state in an Other Matter paragraph that the corresponding figures are unaudited.

The auditor should consider these circumstances using the current year for purposes of comparison and the materiality considerations for the current year. If comparative financial statements are presented, the auditor's opinion should refer to each period for which they are presented and on which an audit opinion is expressed.

165. When reporting on prior period financial statements in connection with the current period audit, if the auditor's current opinion on the prior period financial statements differs from the opinion previously expressed, the auditor should disclose the substantive reasons for the difference in an Other Matters paragraph.
166. If the financial statements of the prior period were audited by a predecessor auditor, in addition to expressing an opinion on the current period financial statements the auditor should state in an Other Matter paragraph:
- that the financial statements of the prior period were audited by the predecessor auditor;
 - the type of opinion expressed by the predecessor auditor and, if the opinion has been modified, the reasons for doing so; and
 - the date of the previous report (unless the predecessor auditor's report on the prior period financial statements is reissued with the present financial statements).

167. If the auditor concludes that the prior period financial statements on which the predecessor auditor reported without modification are affected by a material misstatement, the auditor should communicate the misstatement to the appropriate level of management and those charged with governance and request that the predecessor auditor be informed. If the prior period financial statements are amended and the predecessor auditor agrees to issue a new auditor's report on the amended financial statements, the auditor should report only on the current period.
168. If the prior period financial statements were not audited, the auditor should state in an Other Matter paragraph that the comparative financial statements are unaudited. Doing this does not exempt the auditor from the need to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period financial statements. Further guidance on comparative information is included in ISSAI 1710²⁰.

The auditor's responsibilities in relation to other information in documents containing audited financial statements

169. The auditor should read the other information in order to identify any material inconsistencies or material misstatement of fact with the audited financial statements. If, on reading the other information, the auditor identifies a material inconsistency or material misstatement of fact, the auditor should determine whether the audited financial statements or the other information needs to be revised. The action the auditor should take may include modifying of the auditor's opinion, withholding the auditor's report, withdrawing from the engagement (in the rare cases where this is possible in the public sector), notifying those charged with governance, or including an Other Matter paragraph in the auditor's report.
170. If the auditor identifies a material inconsistency or material misstatement of fact that the management refuses to correct, the auditor is required to notify those charged with governance. Auditors may also be required or decide to notify other parties, such as the legislature, in addition to those charged with governance. Further guidance on the auditor's responsibilities in relation to other documents is included in ISSAI 1720²¹.

Special considerations – audits of financial statements prepared in accordance with special-purpose frameworks

171. The auditor is required to determine the acceptability of the financial reporting framework that was applied when preparing the financial statements. In an audit of special-purpose financial statements, the auditor should obtain an understanding of:
- the purpose for which the financial statements are prepared;
 - the intended users; and
 - the steps taken by management to determine that the applicable financial reporting framework is acceptable in the circumstances.

²⁰ ISSAI 1710 – Comparative Information – Corresponding Figures and Comparative Financial Statements.

²¹ ISSAI 1720 – The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements.

172. In planning and performing an audit of special-purpose financial statements, the auditor should determine whether the circumstances of the engagement require special consideration to be given to application of the ISSAIs.
173. When forming an opinion and reporting on special-purpose financial statements, the auditor should comply with the same requirements as for general-purpose financial statements. The auditor's report on special-purpose financial statements should:
- describe the purpose for which the financial statements have been prepared; and
 - make reference to the management's responsibility for determining that the applicable financial reporting framework is acceptable in the circumstances where the management has a choice of frameworks to use in preparing the financial statements.
174. The auditor should include an Emphasis of Matter paragraph alerting users to the fact that the financial statements have been prepared in accordance with a special-purpose framework and that, as a result, they may not be suitable for another purpose.
175. Further guidance on the special considerations in relation to audits of financial statements prepared in accordance with special-purpose frameworks is included in ISSAI 1800²².

Special considerations – audits of single financial statements and specific elements, accounts or items of a financial statement

176. In the case of an audit of a single financial statement, or of a specific element of a financial statement, the auditor should first determine whether the audit is practicable. The fundamental principles apply to audits of a single financial statement, or of a specific element of a financial statement, irrespective of whether the auditor is also engaged to audit the entity's complete set of financial statements. If the auditor is not also engaged to audit the complete financial statements, the auditor should determine whether the audit of a single financial statement, or of a specific element of those financial statements, is in accordance with the fundamental principles set out in the relevant auditing standards.
177. The auditor should also determine whether application of the financial reporting framework will result in a presentation that provides adequate disclosure to enable the intended users to understand the information in the financial statement or the element thereof, as well as the effect of material transactions and events on that information.
178. The auditor should consider whether the expected form of opinion is appropriate in the circumstances of the engagement, and should adapt the reporting requirements as necessary.
179. If the auditor is engaged to report on a single financial statement, or on a specific element of a financial statement, in conjunction with an engagement to audit the entity's complete set of financial statements, the auditor should express a separate opinion for each engagement.

²² ISSAI 1800 – Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks.

180. If the opinion in the auditor’s report on an entity’s complete financial statements is modified, or the report includes an Emphasis of Matter paragraph or Other Matter paragraph, the auditor should determine the effect this may have on the auditor’s report on a single financial statement or a specific element of a financial statement. Where appropriate, the auditor should modify the opinion or include an Emphasis of Matter paragraph or Other Matter paragraph in the auditor’s report on the single financial statement or specific element of a financial statement.
181. If the auditor concludes that it is necessary to express an adverse opinion or disclaim an opinion on the entity’s complete financial statements, the auditor may not issue an unmodified auditor’s opinion on a single financial statement or a specific element thereof. This is because an unmodified opinion would contradict the adverse opinion or disclaimer of opinion on the financial statements as a whole. Additional requirements and guidance on issuing these reports in conjunction with the opinion on the complete set of financial statements are provided in ISSAI 1805²³.

Considerations relevant to audits of group financial statements (including whole-of-government financial statements)

182. **Auditors engaged to audit group financial statements should obtain sufficient appropriate audit evidence regarding the financial information of all components and the consolidation process to express an opinion as to whether the whole-of-government financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.**
183. The principles of ISSAI 200 apply to all public-sector audits of financial statements, whether for components of government or the whole of government. In situations where the auditor is engaged to audit group financial statements, such as whole-of-government accounts, specific requirements and considerations may apply. The auditor carrying out an audit of group financial statements is referred to as the group auditor. The group auditor should establish a group audit strategy and develop a group audit plan. The principles for understanding the entity should include an understanding of the group, its components and their environments, including group-wide controls, as well as the consolidation process. The understanding thus obtained should be sufficient to confirm or revise the initial identification of components that are likely to be significant for the group financial statements, and to assess the risks of material misstatement, whether due to fraud or error, of the group financial statements.
184. Components of group financial statements may include agencies, departments, bureaus, corporations, funds, component units, districts, joint ventures and non-governmental organisations. Components may be considered to be significant:
- due to their individual financial significance;
 - if, due to their specific nature or circumstances, they are likely to include significant risks of material misstatement of the group financial statements;

²³ ISSAI 1805 – Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement.

- if they involve matters that have heightened public sensitivity, such as national security issues, donor-funded projects or reporting on tax revenue.

185. In the public sector, it can be difficult to decide which components to include in the group financial statements. Application of the financial reporting framework may result in the exclusion of a specific type of agency, department, bureau, corporation, fund, district, joint venture or non-governmental organisation. In such cases, if the group auditor believes that this outcome would result in a misleading presentation of the group financial statements, the group auditor may consider, in addition to the impact on the auditor's report, the need to communicate the matter to the legislature or other appropriate regulatory bodies.
186. In certain situations the financial reporting framework may not provide specific guidance for the inclusion, or exclusion, of a specific type of agency, department, bureau, corporation, fund, district, joint venture or non-governmental organisation in the group financial statements. In such cases, the group auditor may participate in discussions between group management and component management to determine whether the treatment of the component in the group financial statements will result in a fair presentation. This difficulty may have implications for using the work of component auditors. It is also possible that the group management will not agree to include the component in the group financial statements, which may in turn limit the ability of the group auditor to communicate with and use the work of the component auditor.
187. In the case of a component that is significant due to its individual financial significance within the group, the group audit team, or a component auditor on its behalf, should audit the financial information of the component using a component materiality value set by the group auditor. For a component that is significant due to its specific nature or circumstances and because it is likely to mean significant risks of material misstatement of the group financial statements, the group audit team, or a component auditor on its behalf, may not need to audit the financial information but may apply specified audit procedures relating to the significant risks identified. In the case of components that are not significant, the group audit team should perform analytical procedures at group level.
188. When developing or adopting auditing standards based on, or consistent with, the Fundamental Principles of Financial Auditing, it may be useful to consider the detailed guidance on group audits in ISSAI 1600²⁴.

²⁴ ISSAI 1600 – Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors).