

**PROPOSED INTERNATIONAL STANDARD ON ASSURANCE  
ENGAGEMENTS 3402****Assurance Reports on Controls at a Third Party Service Organization**

Includes proposed conforming amendments to “Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services.”

**Introduction****Scope of this ISAE**

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

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<sup>1</sup> [Proposed] ISA 402 (Revised and Redrafted), “Audit Considerations Relating to an Entity Using a Third Party Service Organization.”

*Relationship with Other Professional Pronouncements*

5. The service auditor is required by paragraph 11 of this ISAE to comply with ISAE 3000<sup>2</sup> in addition to this ISAE. The Assurance Framework, which defines and describes the elements and objectives of an assurance engagement, provides the context for understanding this ISAE and ISAE 3000.
6. Compliance with ISAE 3000 requires, among other things, that the service auditor comply with the Code of Ethics for Professional Accountants (the Code), and implement quality control procedures that are applicable to the individual engagement.

**Effective Date**

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

**Objectives**

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

**Definitions**

9. For purposes of this ISAE, the following terms have the meanings attributed below:
  - (a) Carve-out Method – Method of dealing with the services provided by a subservice organization, whereby the service organization's description of its system includes the nature of the activities performed by a subservice organization, but that subservice organization's relevant control objectives and related controls are excluded from the service organization's description of the system and from the scope of the service auditor's engagement. The service organization's description of the system and the scope of the service auditor's engagement include controls at the service organization to monitor the effectiveness of controls at the subservice organization, which may include the service organization's review of a Type B or Type A report on controls at the subservice organization.
  - (b) Complementary User Entity Controls – Controls that the service organization assumes, in the design of its service, will be implemented by user entities, and which, if necessary to achieve control objectives, are identified in the description of the system.

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<sup>2</sup> ISAE 3000, "Assurance Engagements Other than Audits or Reviews of Historical Financial Information."

- (c) Control Objectives – The aim or purpose of a particular aspect of controls at the service organization. Control objectives ordinarily relate to risks that controls seek to mitigate.
- (d) Controls at Service Organization– The process designed, implemented and maintained by the service organization to provide reasonable assurance about the achievement of the control objectives that are relevant to services covered by the service auditor’s assurance report and that are likely to be relevant to user entities’ internal control as it relates to financial reporting. (Ref: Para. A1)
- (e) Controls at Subservice Organization– The process designed, implemented and maintained by the subservice organization to provide reasonable assurance about the achievement of the control objectives that are relevant to the services covered by the service auditor’s assurance report.
- (f) Criteria – Benchmarks used to evaluate or measure a subject matter including, where relevant, benchmarks for presentation and disclosure. Suitable criteria are required for reasonably consistent evaluation or measurement of a subject matter within the context of professional judgment. Criteria need to be available to the intended users to allow them to understand how the subject matter has been evaluated or measured. See paragraphs 14-16 for minimum elements encompassed by criteria that are suitable for engagements to report on controls at a third party service organization.
- (g) Inclusive Method – Method of dealing with the services provided by a subservice organization, whereby the service organization’s description of its system includes the nature of the services performed by a subservice organization, and that subservice organization’s relevant control objectives and related controls are included in the service organization’s description of the system and in the scope of the service auditor’s engagement.
- (h) Report on the Description and Design of Controls at a Service Organization (referred to in this ISAE as a “Type A report”) – A report that comprises:
  - (i) A description of the service organization’s system prepared by management of the service organization;
  - (ii) A written assertion by the service organization’s management that, in all material respects, and based on suitable criteria:
    - (a) The description fairly presents the service organization’s system that had been designed and implemented as at a specified date;
    - (b) The controls related to the control objectives included in the description were suitably designed as at the specified date; and
  - (iii) A service auditor’s assurance report that conveys reasonable assurance about the matters in (ii) (a) and (b) above.
- (i) Report on the Description, Design and Operating Effectiveness of Controls at a Service Organization (referred to in this ISAE as a “Type B report”) – A report that comprises:

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

## **Requirements**

### **ISAE 3000**

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

### **Ethical Requirements**

11. As required by the Code, the service auditor shall be independent from the service organization. However, in performing an engagement in accordance with this ISAE, the Code does not require the service auditor to be independent from each user entity.

### **Acceptance and Continuance**

12. The service auditor shall accept (or continue where applicable) an engagement only if:
- (a) The service auditor's preliminary knowledge of the engagement circumstances indicates that:
    - (i) The criteria to be used will be suitable and available to the intended users;
    - (ii) The service auditor will have access to sufficient appropriate evidence to the extent necessary; and
    - (iii) The description of the system included in the scope of the engagement will not be so limited that it is unlikely that the engagement has a rational purpose; (Ref: Para. A2)
  - (b) In agreeing the terms of the engagement, the service organization acknowledges that it understands and accepts its responsibility for:
    - (i) Preparing and presenting the description of the system and accompanying assertions, including the completeness, accuracy and method of presentation of the description and assertions;
    - (ii) Developing the control objectives (where not specified by law or regulation, or another party, for example a user group or a professional body), and identifying the risks that threaten their achievement;
    - (iii) Designing, implementing and maintaining controls to achieve the identified control objectives; and
    - (iv) Providing complete information to the service auditor in connection with the engagement.

### **Assessing the Suitability of the Criteria**

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

14. Suitable criteria for evaluating whether the description of the system is fairly presented shall encompass at a minimum whether the description:
  - (a) Presents how the service organization's system made available to user entities has been designed and implemented to process relevant transactions, including, as appropriate:
    - (i) The classes of transactions processed;
    - (ii) The procedures, within both information technology and manual systems, by which transactions are initiated, recorded, processed, corrected as necessary, and transferred to the reports presented to user entities;
    - (iii) The related accounting records, supporting information and specific accounts that are used to initiate, record, process and report transactions; this includes the correction of incorrect information and how information is transferred to the reports presented to user entities;
    - (iv) How the service organization's system captures significant events and conditions, other than transactions;
    - (v) The process used to prepare reports presented to user entities; and
    - (vi) Other aspects of the service organization's control environment, risk assessment process, information system (including the related business processes) and communication, control activities and monitoring controls that are relevant to achieving the control objectives; and
  - (b) Does not omit or distort information relevant to the scope of the service organization's system being described, while acknowledging that the description is presented to meet the common needs of a broad range of user entities and may not, therefore, include every aspect of the service organization's system that each individual user entity may consider important in its particular environment.
15. Suitable criteria for evaluating whether controls are suitably designed shall encompass at a minimum whether:
  - (a) The risks that threaten achievement of the control objectives included in the description have been identified; and
  - (b) The identified controls would, if operated as described, provide reasonable assurance that those risks do not prevent the control objectives from being achieved.
16. Suitable criteria for evaluating whether controls have operated effectively shall encompass at a minimum whether the controls were consistently applied as designed. This includes whether manual controls were applied by individuals who have the appropriate competence and authority. (Ref: Para. A3)

## **Materiality**

17. As required by ISAE 3000, the service auditor shall consider materiality and assurance engagement risk when planning and performing the engagement. (Ref: Para. A4)

## Using the Work of an Internal Audit Function

### *Obtaining an Understanding of the Internal Audit Function*

18. The service auditor shall obtain an understanding of the aspects of the internal audit function<sup>3</sup> that are relevant to the engagement. (Ref: Para. A5-A6)

### *Planning to Use the Work of the Internal Audit Function*

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

### *Using the Work of the Internal Audit Function*

21. When the service auditor uses specific work of the internal audit function, the service auditor shall perform procedures to evaluate the adequacy of that work.
22. When evaluating specific work performed by the internal audit function, the service auditor shall consider the adequacy of the scope of work and whether the evaluation of the internal audit function remains appropriate. The service auditor shall evaluate whether:
- (a) The work is performed by persons having appropriate skills and expertise;
  - (b) The work is properly supervised, reviewed and documented;
  - (c) Sufficient appropriate evidence is obtained to be able to draw reasonable conclusions;
  - (d) Conclusions reached are appropriate in the circumstances and any reports prepared are consistent with the results of the work performed; and
  - (e) Any exceptions or unusual matters disclosed by the internal audit function are properly resolved.

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<sup>3</sup> As used in this ISAE, the term "internal audit function" also includes others (by whatever name, e.g., a compliance or risk department) who perform similar activities to internal audit functions (see A5).

*Effect on the Service Auditor's Assurance Report*

23. If the work of the internal audit function has been used, the service auditor shall make no reference to that work in the section of the service auditor's assurance report that contains the service auditor's opinion. (Ref: Para. A7)
24. In the case of a Type B report, if the work of the internal audit function has been used in performing tests of controls, that part of the service auditor's assurance report that describes the service auditor's tests of controls and the results thereof shall include a description of the internal auditor's work and of the service auditor's procedures with respect to that work.

**Using the Work of a Service Auditor's External Expert**

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

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

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

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

*Agreement with the Service Auditor's Expert*

27. The service auditor shall agree, in writing when appropriate, the following matters with the service auditor's expert:
  - (a) The nature, scope and objectives of that expert's work;
  - (b) The respective roles of the service auditor and that expert; and
  - (c) The nature, timing and extent of communication between the service auditor and that expert, including the form of any report to be provided by that expert.

*Evaluating the Adequacy of the Service Auditor's Expert's Work*

28. The service auditor shall evaluate the adequacy of the service auditor's expert's work for the purposes of the engagement.

*Effect on the Service Auditor's Assurance Report*

29. If the work of a service auditor's external expert has been used, the service auditor shall make no reference to that work in the section of the service auditor's assurance report that contains the service auditor's opinion. (Ref: Para. A7)



30. In the case of a Type B report, if the work of a service auditor's external expert has been used in performing tests of controls, that section of the service auditor's assurance report that describes the service auditor's tests of controls and the results thereof shall include a description of the service auditor's external expert's work and of the service auditor's procedures with respect to that work.

### **Obtaining an Understanding of the Service Organization's System**

31. The service auditor shall obtain an understanding of the service organization's system, including controls, provided by the service organization that are included in the scope of the engagement. (Ref: Para. A8-A9)

### **Obtaining Evidence Regarding the Description**

32. The service auditor shall obtain and read the service organization's description of the system, and shall evaluate whether those aspects of the description included in the scope of the engagement are free from material misstatement, including whether: (Ref: Para. A10-A11)
- (a) Specified control objectives are reasonable in the circumstances; (Ref: Para. A12)
  - (b) Controls identified in the description were implemented;
  - (c) Complementary user entity controls, if any, are adequately described; and
  - (d) Services performed by a subservice organization, if any, are adequately described, including whether the inclusive method or the carve-out method has been used in relation to them. (Ref: Para. A13)
33. The service auditor shall confirm the implementation of the service organization's system through other procedures in combination with inquiries of management and other service organization personnel. Those other procedures shall include observation, and inspection of records and other documentation, of the manner in which transactions are processed through the system and controls are applied. (Ref: Para. A13)

### **Obtaining Evidence Regarding Design of Controls**

34. The service auditor shall determine which of the controls at the service organization are necessary to achieve the control objectives included in the scope of the engagement, and shall assess whether those controls were suitably designed. This shall include: (Ref: Para. A14-A16)
- (a) Identifying the risks that threaten the achievement of the specified control objectives included in the scope of the engagement; and
  - (b) Evaluating the linkage of controls identified in the description with those risks.

### **Obtaining Evidence Regarding Effectiveness of Controls**

35. If providing a Type B report, the service auditor shall test those controls that the service auditor has determined are necessary to achieve the control objectives included in the scope of the engagement, and assess their operating effectiveness. (Ref: Para. A17-A22)
36. When designing and performing tests of controls, the service auditor shall:
- (a) Perform other procedures in combination with inquiry to obtain evidence about:

- (i) How the control was applied;
    - (ii) The consistency with which the control was applied; and
    - (iii) By who or by what means the control was applied;
  - (b) Determine whether controls to be tested depend upon other controls (indirect controls), and if so, whether it is necessary to obtain evidence supporting the operating effectiveness of those indirect controls; and
  - (c) Determine means of selecting items for testing that are effective in meeting the objectives of the procedure. (Ref: Para. A23-A24)
37. When determining the extent of tests of controls, the service auditor shall consider the characteristics of the population from which the sample will be drawn, including the nature of controls, the frequency of their application ( for example, monthly, daily, a number of times per day), and the expected rate of deviation.

*Sampling*

38. When the service auditor uses sampling, the service auditor shall:
- (a) Determine a sample size sufficient to conclude with an appropriately low level of sampling risk that the total rate of deviation does not exceed the tolerable rate of deviation; (Ref: Para. A25)
  - (b) Select items for the sample in such a way that all sampling units in the population have a chance of selection;
  - (c) If a designed procedure is not applicable to a selected item, perform the procedure on a replacement item; and
  - (d) If unable to apply the designed procedures, or suitable alternative procedures, to a selected item, treat that item as a deviation.

*Nature and Cause of Deviations*

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

representative of the population. The service auditor shall obtain this degree of certainty by performing additional procedures to obtain sufficient appropriate evidence that such deviations do not exist in the remainder of the population.

### **Written Representations**

41. The service auditor shall request management or those charged with governance to provide written representations based on their knowledge and belief, having made appropriate inquiries for them to be able to provide such representations: (Ref: Para. A26-A27)
  - (a) That reaffirm the assertions accompanying the description of the system;
  - (b) Whether all records, documentation, unusual matters of which they are aware, and other information relevant to the assurance engagement have been made available to the service auditor; and
  - (c) That they have disclosed to the service auditor any of the following of which they are aware:
    - Non-compliance with laws and regulations, or uncorrected errors attributable to the service organization's management or employees that may affect one or more user entities;
    - Design deficiencies in controls, including those for which management believes the cost of corrective action may exceed the benefits;
    - Instances where controls have not operated as described; and
    - Subsequent events regarding the services covered by the engagement that could have a significant effect on user entities.
42. These written representations noted, shall be in the form of a representation letter addressed to the service auditor, and shall be as of the same date as the service auditor's assurance report.
43. If management does not provide the written representations requested by the service auditor, the auditor shall:
  - (a) Ask for the reasons;
  - (b) Reconsider the assessment of the integrity of management; and
  - (c) Take appropriate actions, including determining the possible effects on the opinion in the service auditor's assurance report.

### **Other Information**

44. The service auditor shall read the other information, if any, included in a document containing the description of the system that is provided to user entities on the same terms and at the same time as the description of the system, to identify material inconsistencies, if any, with that description. While reading the other information for the purpose of identifying material inconsistencies, the service auditor may become aware of an apparent misstatement of fact.

45. If the service auditor becomes aware of a material inconsistency or an apparent misstatement of fact, the service auditor shall discuss the matter with management. If the service auditor concludes that there is a material inconsistency or a misstatement of fact that management refuses to correct, the service auditor shall take further appropriate action.

### **Subsequent Events**

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

### **Documentation**

48. The service auditor shall prepare documentation so as to enable an experienced service auditor, having no previous connection with the engagement, to understand:
  - (a) The nature, timing, and extent of the procedures performed to comply with this ISAE and applicable legal and regulatory requirements;
  - (b) The results of the procedures and the evidence obtained; and
  - (c) Significant matters arising during the engagement, and the conclusions reached thereon and significant professional judgments made in reaching those conclusions.
49. In documenting the nature, timing and extent of procedures performed, the service auditor shall record:
  - (a) The identifying characteristics of the specific items or matters being tested;
  - (b) Who performed the procedures and the date such procedures were completed; and
  - (c) Who reviewed the work performed and the date and extent of such review.
50. The service auditor shall document discussions of significant matters with the service organization and others including when and with whom the discussions took place.
51. If the service auditor has identified information that is inconsistent with the service auditor's final conclusion regarding a significant matter, the service auditor shall document how the service auditor addressed the inconsistency in forming the final conclusion.
52. The service auditor shall complete the assembly of the final engagement file on a timely basis after the date of the service auditor's assurance report.
53. After the assembly of the final engagement file has been completed, the service auditor shall not delete or discard audit documentation before the end of its retention period. (Ref: Para. A28)

54. If the service auditor finds it necessary to modify existing engagement documentation or add new documentation after the assembly of the final engagement file has been completed, the service auditor shall, regardless of the nature of the modifications or additions, document:
- (a) When and by whom they were made, and (where applicable) reviewed;
  - (b) The specific reasons for making them; and
  - (c) Their effect, if any, on the service auditor's conclusions.

### **Preparing the Service Auditor's Assurance Report**

#### *Service Auditor's Assurance Report Content*

55. The service auditor's assurance report shall include the following basic elements (Ref: Para. A29):
- (a) A title that clearly indicates the report is an independent service auditor's assurance report.
  - (b) An addressee.
  - (c) Identification of:
    - (i) The description of the system, and management's assertion, which includes the matters described in paragraph 10(h)(ii) for a Type B report, or paragraph 10(i)(ii) for a Type A report.
    - (ii) If parts of the description of the system are not covered by the service auditor's opinion, an identification of those parts;
    - (iii) If the description includes complementary user entity controls, a statement that the service auditor has not evaluated the operating effectiveness of complementary user entity controls, and that if complementary user entity controls are not operating effectively, controls at the service organization cannot be expected to achieve the specified objectives; and
    - (iv) If services are performed by a subservice organization, those services and whether the inclusive method or the carve-out method has been used in relation to them. Where the carve-out method has been used, a statement that the description of the system excludes the control objectives and related controls at relevant subservice organizations, and that the service auditor's procedures do not extend to the subservice organization. Where the inclusive method has been used, a statement that the description of the system includes the control objectives and related controls at the subservice organization, and that the service auditor's procedures included the subservice organization.
  - (d) Identification of the criteria, and the party specifying the control objectives.
  - (e) A statement of the limitations of controls and, in the case of a Type B report, of the risk of projecting to future periods any evaluation of the effectiveness of controls.

- (f) Identification of the purpose(s) and intended users of the service auditor's assurance report. (Ref: Para. A30)
- (g) A description of the service organization's and the service auditor's responsibilities, including a statement that the service organization is responsible for:
  - (i) Preparing and presenting the description of the system, and accompanying assertions, including the completeness, accuracy and method of presentation of the description and assertions;
  - (ii) Providing the services covered by the description of the system;
  - (iii) Identifying the control objectives (where not identified by law or regulation, or another party, for example a user group or a professional body), and the risks that threaten their achievement; and
  - (iv) Designing, implementing and maintaining controls to achieve the identified control objectives.
- (h) A statement that the engagement was performed in accordance with ISAE 3402, "Assurance Reports on Controls at a Third Party Service Organization."
- (i) A summary of the service auditor's procedures to obtain reasonable assurance and, in the case of a Type A report, a statement that the service auditor has not performed any procedures regarding the operating effectiveness of controls and therefore no opinion is expressed thereon.
- (k) The service auditor's opinion, expressed in the positive form, on whether, in all material respects, based on suitable criteria:
  - (i) In the case of a Type B report:
    - The description fairly presents the service organization's system that had been designed and implemented throughout the specified period;
    - The controls related to the control objectives included in the description were suitably designed throughout the specified period; and
    - The controls the service auditor tested operated effectively throughout the specified period.
  - (ii) In the case of a Type A report:
    - The description fairly presents the service organization's system that had been designed and implemented as at the specified date; and
    - The controls related to the control objectives included in the description were suitably designed as at the specified date.
- (l) The date of the service auditor's assurance report.
- (m) The name of the service auditor, and the city where the service auditor maintains the office that has responsibility for the engagement.

56. In the case of a Type B report, the service auditor's assurance report shall include a separate section or attachment that describes the service auditor's tests of controls and the results thereof. In describing the tests of controls, the auditor shall clearly state which controls have been tested and the period during which they were tested, identify whether the items tested represent all or a selection of the items in the population, and indicate the nature of the tests in sufficient detail to enable user auditors to determine the effect of such tests on their risk assessments. If deviations have been identified, the service auditor shall include:

- (a) Information about causative factors, to the extent the service auditor has identified such factors; and
- (b) The extent of testing performed by the service auditor that led to identification of the deviations, and the number of deviations noted.

The service auditor shall report deviations even if, on the basis of tests performed, the service auditor has concluded that the related control objective has been achieved. (Ref: Para. A31)

#### *Modified Opinions*

57. If the service auditor concludes that:

- (a) Management's description of the system is not presented fairly in all material respects;
- (b) The controls are not suitably designed to provide reasonable assurance that the specified control objectives will be achieved if the controls operate effectively;
- (c) In the case of a Type B report, the controls did not operate effectively throughout the specified period; or
- (d) The service auditor is unable to obtain sufficient appropriate evidence,

the service auditor's opinion shall be modified, and the service auditor's assurance report shall contain a clear description of all the reasons for the modification. (Ref: Para. A32)

#### **Other Reporting Responsibilities**

58. If the service auditor becomes aware of non-compliance with laws and regulations, or uncorrected errors attributable to the service organization that are not clearly trivial and may affect one or more user entities, the service auditor shall determine whether this information has been communicated appropriately to affected user entities. If the information has not been so communicated and management of the service organization is unwilling to do so, the service auditor shall take appropriate action. (Ref: Para. A33)

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## **Application and Other Explanatory Material**

### **Definitions** (Ref: Para. 10(d))

A1. The process referred to in the definition of "controls at service organization" at paragraph 10(d) invariably includes aspects of user entities' information systems maintained by the service organization, and may also include aspects of one or more of the other components of

internal control. For example, it may include aspects of the service organization’s control environment, monitoring, and control activities where they relate to the services provided. It does not, however, include controls at a service organization that are not related to the achievement of the control objectives specified in the description of the system, for example controls related to the preparation of the service organization’s own financial statements.

**Acceptance and Continuance** (Ref: Para. 12(a)(iii))

- A2. A request not to include certain aspects of controls at the service organization from the scope of the engagement may not have a reasonable justification when, for example, the request is made because of the likelihood that the service auditor’s opinion would be modified with respect to those aspects.

**Assessing the Suitability of the Criteria** (Ref: Para. 13-17)

- A3. ISAE 3000 requires the service auditor, amongst other things, to assess the suitability of criteria, and the appropriateness of the subject matter. The subject matter is the underlying condition of interest to intended users of an assurance report. The following table identifies the subject matter and minimum criteria for each of the opinions in Type B and Type A reports.

	<i>Subject matter</i>	<i>Criteria</i>	<i>Comment</i>
<i>Opinion about the fair presentation of the description of the system (Type A and Type B reports)</i>	The system that is relevant to services covered by the service assurance auditor’s report.	The description is fairly presented if it: (a) Presents how the service organization’s system made available to user entities has been designed and implemented to process relevant transactions including the matters identified in para 14 (a); and (b) Does not omit or distort information relevant to the scope of the service organization’s system being described, while acknowledging that the description is presented to meet the common needs of a broad range of user entities and may not, therefore, include every aspect of the service organization’s system that each individual user entity may consider	The specific wording of the criteria for this opinion may need to be tailored to be consistent with criteria established by, for example, law or regulation, user groups, or a professional body. Examples of criteria for this opinion are provided in the illustrative assertions in Appendix 2. Paragraphs A10-A13 offer further guidance on determining whether these criteria are met. (In terms of ISAE 3000, the subject matter information <sup>4</sup> for this opinion is the description of the system and the service organization’s assertion that the description is presented fairly).

<sup>4</sup> The “subject matter information” is the outcome of the evaluation or measurement of the subject matter that results from applying the criteria to the subject matter.



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

**Materiality** (Ref: Para. 17)

- A4. The service auditor's consideration of materiality includes both quantitative and qualitative matters. Considering materiality with respect to the fair presentation of the description, and with respect to the design of controls, is primarily directed at qualitative matters, for example, whether the description includes the significant aspects of processing significant transactions, whether the description omits or distorts relevant information, and the ability of

controls, as designed, to provide reasonable assurance that that control objectives would be achieved. Matters that influence the consideration of materiality with respect to the operating effectiveness of controls include both quantitative and qualitative factors, for example, the tolerable rate and observed rate of deviation (a quantitative matter), and the nature and cause of any observed deviation (a qualitative matter).

## **Using the Work of an Internal Audit Function**

### *Obtaining an Understanding of the Internal Audit Function* (Ref: Para. 18)

- A5. As used in this ISAE, “internal audit function” also includes others (by whatever name, for example, a compliance or risk department) who perform similar activities to the internal audit function. An internal audit function may be responsible for providing analyses, evaluations, assurances, recommendations, and other information to management and those charged with governance. An internal audit function at a service organization may perform activities related to the service organization’s internal control, or activities related to the services and systems, including controls, that the service organization is providing to user entities.
- A6. The scope and objectives of an internal audit function vary widely and depend on the size and structure of the service organization and the requirements of management and those charged with governance. Internal audit function activities may include one or more of the following:
- Monitoring of the service organization’s internal control or the application processing systems, including controls, provided to user entities. The internal audit function may be assigned specific responsibility for reviewing controls, monitoring their operation and recommending improvements thereto.
  - Examination of financial and operating information. The internal audit function may be assigned to review the means used to identify, measure, classify and report financial and operating information, and specific inquiry and other procedures into individual items including detailed testing of transactions, balances and procedures.
  - Evaluation of the economy, efficiency and effectiveness of operating activities including non-financial activities of a service organization.
  - Evaluation of compliance with laws, regulations and other external requirements, and with management policies and directives and other internal requirements.

### *Effect on the Service Auditor’s Assurance Report* (Ref: Para. 23 and para. 29)

- A7. Notwithstanding its degree of autonomy and objectivity, the internal audit function is not independent of the service organization. The service auditor has sole responsibility for the opinion expressed in the service auditor’s assurance report and, accordingly, that responsibility is not reduced by the service auditor’s use of the work of the internal audit function.

**Obtaining an Understanding of the Service Organization's System** (Ref: Para. 31)

- A8. Obtaining an understanding of the service organization's system, including controls, included in the scope of the engagement, assists the service auditor in:
- Identifying the boundaries of the system, and how it interfaces with others systems.
  - Assessing whether the service organization's description fairly presents the system that has been designed and implemented.
  - Determining which controls are necessary to achieve the control objectives included in the scope of the engagement, and whether controls were suitably designed, and, in the case of a Type B report, operating effectively.
- A9. Procedures to obtain this understanding may include:
- Inquiring of management, and of others within the service organization who in the service auditor's judgment may have relevant information.
  - Observation of operations, and inspection of documents, reports, printed and electronic records of transaction processing.
  - Inspecting a selection of agreements between the service organization and user entities to identify their common terms.

**Obtaining Evidence Regarding the Description** (Ref: Para. 32-33)

- A10. Considering the following questions may assist the service auditor in determining whether those aspects of the description included in the scope of the engagement are free from material misstatement:
- Does the description address the major aspects of the service provided (within the scope of the engagement) that could reasonably be expected to be relevant to the common needs of a broad range of user auditors in planning their audits of user entities' financial statements?
  - Is the description presented at a level of detail that could reasonably be expected to provide a broad range of user auditors with sufficient information to obtain an understanding of internal control in accordance with ISA 315 (Redrafted)?<sup>5</sup> The description need not address every aspect of the service organization's processing or the services provided to user entities, and need not be so detailed as to potentially allow a reader to compromise security or other controls at the service organization.
  - Is the description prepared and presented in a manner that does not omit or distort information that may affect the common needs of a broad range of user auditors'?

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<sup>5</sup> ISA 315 (Redrafted), "Identifying and Assessing Risks of Material Misstatement Through Understanding the Entity and Its Environment."

decisions, for example, does the description objectively describe any significant omissions or inaccuracies in processing of which the service auditor is aware?

- Have the controls identified in the description actually been implemented?
- Are complementary user entity controls, if any, adequately described? In most cases, the description of control objectives is worded such that the control objectives are capable of being achieved through effective operation of controls implemented by the service organization alone. In some cases, however, the control objectives specified in the description cannot be achieved by the service organization alone because their achievement requires particular controls to be implemented by user entities. This may be the case where, for example, the control objectives are specified by a regulatory authority. When the description does include complementary user entity controls, the description separately identifies those controls.

A11. The service auditor's procedures to evaluate the fair presentation of the description may include:

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

A12. Paragraph 32 (a) requires the service auditor to evaluate whether the specified control objectives are reasonable in the circumstances. Considering the following questions may assist the auditor in this evaluation:

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

- A13. If the inclusive method has been used, it is important that the description adequately differentiates between controls at the service organization and controls at the subservice organization. If the carve-out method is used, it is important that the description identifies the functions that are performed by the subservice organization, but it need not describe the detailed processing or controls at the subservice organization.

**Obtaining Evidence Regarding the Design of Controls** (Ref: Para. 34)

- A14. From the viewpoint of a *user auditor*, a control is suitably designed if individually or in combination with other controls, it would, when complied with satisfactorily, provide reasonable assurance that material misstatements, whether due to fraud or error, are prevented, or detected and corrected. A *service auditor*, however, is not aware of the circumstances at individual user entities that would determine whether or not a misstatement resulting from a control deviation is material to those user entities. Therefore, from the viewpoint of a service auditor, a control is suitably designed if individually or in combination with other controls, it would, when complied with satisfactorily, provide reasonable assurance that control objectives are achieved.
- A15. A service auditor may consider using flowcharts, questionnaires, or decision tables to facilitate understanding the design of the controls.
- A16. Controls may consist of a number of integrated activities directed at the achievement of various control objectives. Consequently, where the service auditor evaluates certain activities as being ineffective in achieving a particular control objective, the existence of other activities, sometimes known as compensating controls, may nonetheless allow the service auditor to conclude that controls related to the control objective are suitably designed.

**Obtaining Evidence Regarding the Effectiveness of Controls**

*Assessing Operating Effectiveness* (Ref: Para. 35)

- A17. From the viewpoint of a *user auditor*, a control is operating effectively if individually or in combination with other controls, it provides reasonable assurance that material misstatements, whether due to fraud or error, are prevented, or detected and corrected. A *service auditor*, however, is not aware of the circumstances at individual user entities that would determine whether or not a misstatement resulting from a control deviation is material. Therefore, from the viewpoint of a service auditor, a control is operating effectively if individually or in combination with other controls, it provides reasonable assurance that specified control objectives are achieved. Similarly, a service auditor is not in a position to determine whether any observed control deviation would result in a material misstatement from the viewpoint of an individual user entity.
- A18. Obtaining an understanding of controls sufficient to opine on their design effectiveness is not sufficient evidence regarding their operating effectiveness, unless there is some automation that provides for the consistent operation of the controls as they were designed and implemented. For example, obtaining information about the implementation of a manual control at a point in time does not provide evidence about operation of the control at other times. However, because of the inherent consistency of IT processing, performing procedures

to determine the design of an automated control and whether it has been implemented may serve as evidence of that control's operating effectiveness, depending on the service auditor's assessment and testing of other controls, such as those over program changes.

- A19. To be useful to user auditors, a Type B report ordinarily covers a minimum period of six months. If the period is less than six months, the service auditor may consider it appropriate to describe the reasons for the shorter period in the service auditor's assurance report. Circumstances that may result in a report covering a period of less than six months include when (a) the service auditor is engaged close to the date by which the report on controls is to be issued; (b) the service organization (or a particular system or application) has been in operation for less than six months; or (c) significant changes have been made to the controls and it is not practicable either to wait six months before issuing a report or to issue a report covering the system both before and after the changes.
- A20. Certain control procedures may not leave evidence of their operation that can be tested at a later date and accordingly, the service auditor may find it appropriate to test the operating effectiveness of such control procedures at various times throughout the reporting period.
- A21. Unlike in a financial statement audit, evidence from prior engagements about the satisfactory operation of controls in prior periods cannot provide a basis for a reduction in testing, even if it is supplemented with evidence obtained during the current period. This is because in a service organization engagement, the service auditor provides an opinion on the effectiveness of controls throughout each period, therefore sufficient evidence about the operation of controls during the current period is required for the service auditor to express that opinion.
- A22. Where the service organization implemented changes to its control procedures during the period covered by the service auditor's engagement, for example, to improve the efficiency of controls or to address identified deficiencies, the impact the superseded control procedures had on achievement of control objectives during the period may still be relevant. Where a change of controls occurs during the period, the service auditor may seek to agree with management whether it is possible for the controls to be tested before and after the change.

*Means of Selecting Items for Testing* (Ref: Para. 36(c))

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

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

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

*Sample size* (Ref: Para. 38(a))

A25. When attribute sampling is used in relation to controls at a service organization for which no deviations are expected, it is not uncommon for service auditors to use a sample size of 25 to approximate a statistically calculated sample size based on a large population with a 90% confidence that there is less than a 10% rate of deviation.

**Written Representations** (Ref: Para. 41-43)

A26. The written representations reconfirming the service organization's assertion about the effective operation of controls may be based on ongoing monitoring activities, separate evaluations, or a combination of the two. Ongoing monitoring activities are often built into the normal recurring activities of a service organization and include regular management and supervisory activities. Internal auditors or personnel performing similar functions may contribute to the monitoring of a service organization's activities. Monitoring activities may also include using information from communications from external parties, such as customer complaints and regulator comments, that may indicate problems or highlight areas in need of improvement.

A27. The written representations required by paragraph 41 are separate from, and in addition to the assertion contained in the service organization's report on controls, as described in paragraph 9 (i)(ii) for a Type B report, and paragraph 9 (h)(ii) for a Type A report.

**Documentation** (Ref: Para. 53)

A28. [Proposed] ISQC 1 (Redrafted), "Quality Control for firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements" requires firms to establish policies and procedures for the retention of engagement documentation. The retention period for service audit engagements ordinarily is no shorter than five years from the date of the service auditor's assurance report.

**Preparing the Service Auditor's Assurance Report**

*Content of the Service Auditor's Assurance Report* (Ref: Para.55)

A29. Illustrative examples of service auditors' assurance reports and related service organization's management assertions are contained in Appendices 1 and 2.

*Use of the Service Auditor's Assurance Report* (Ref: Para. 55(f))

A30. It may be appropriate to include a statement that use of the service auditor's assurance report is intended for specific users or for a specific purpose(s). This may be the case when, for example, the service auditor's assurance report is likely to be misunderstood by readers who

do not have a level of practical understanding of the service organization's system that can reasonably be expected of only existing users and their financial statement auditors.

*Description of the Service Auditor's Tests of Controls* (Ref: Para. 56)

A31. In describing the nature of the service auditor's tests of controls for a Type B report, it assists readers if the service auditor's assurance report defines the types of tests performed. It also assists readers of the service auditor's report if the service auditor includes the results of all tests where deviations have been identified, even if compensating controls have been identified or the control tested has subsequently been removed from the description of the system.

*Modified Opinions* (Ref: Para. 57)

A32. Illustrative examples of elements of modified service auditor's assurance reports are contained in Appendix 3.

**Other Reporting Responsibilities** (Ref: Para. 58)

A33. Appropriate action when the service auditor becomes aware of non-compliance with laws and regulations, or uncorrected error that has not been communicated appropriately to affected user entities, and management of the service organization is unwilling to do so, may include:

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



**Appendix 1**

(Ref. Para. A29)

**Example Management Assertions**

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

**EXAMPLE 1: Type B Assertion for Service Organization****Management's Assertion**

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

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

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

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

*[Management (or Those Charged With Governance)]*

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**EXAMPLE 2: Type A Assertion for Service Organization****Management's Assertion**

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

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

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

*[Management (or Those Charged With Governance)]*

### **Example Service Auditor's Assurance Reports**

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

#### **EXAMPLE 1: Type B Service Auditor's Assurance Report**

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

To: XYZ Service Organization

###### *Scope*

We have conducted an assurance engagement to report on XYZ Service Organization's description at pages [bb-cc] of [the type or name of] system made available to customers for processing their transactions throughout the period [date] to [date] (the description), and on the design and operation of controls related to the control objectives included in the description.<sup>6</sup>

###### *Management's Responsibilities*

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

###### *Service Auditor's Responsibilities*

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

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<sup>6</sup> If some elements of the description are not included in the scope of the engagement, this is made clear in the assurance report.

An assurance engagement on the description, design and effective operation of controls at a service organization involves performing procedures to obtain evidence about the disclosures in the description of the system, and the design and effective operation of controls. The procedures selected depend on the service auditor's judgment, including the assessment of the risks of material misstatement of the description, and the risks of material deficiencies in design or operation of the controls, whether due to fraud or error. An assurance engagement of this type also includes evaluating the overall presentation of the description, and the suitability of the objectives included therein.

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

#### *Limitations of Internal Controls at a Service Organization*

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

#### *Opinion*

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

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

#### *Description of Tests of Controls*

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

#### *Intended Users and Purpose*

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

[Service auditor's signature]

[Date of the service auditor's assurance report]

[Service auditor's address]

## **EXAMPLE 2: Type A Service Auditor's Assurance Report**

### **Independent Service Auditor's Assurance Report on the Description of Controls and their Design**

To: XYZ Service Organization

#### *Scope*

We have conducted an assurance engagement to report on XYZ Service Organization's description at pages [bb-cc] of [the type or name of] system made available to customers for processing their transactions as at [date] (the description), and on the design of controls related to the control objectives included in the description.<sup>7</sup>

#### *Management's Responsibilities*

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

#### *Service Auditor's Responsibilities*

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

An assurance engagement on the description and design of controls at a service organization involves performing procedures to obtain evidence about the disclosures in the description of the system, and the design of controls. The procedures selected depend on the service auditor's judgment, including the assessment of the risks of material misstatement of the description, and the risks of material deficiencies in design of the controls, whether due to fraud or error. An assurance engagement of this type also includes evaluating the overall presentation of the description, and the suitability of the objectives included therein.

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

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<sup>7</sup> If some elements of the description are not included in the scope of the engagement, this is made clear in the assurance report.

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

*Limitations of Internal Controls at a Service Organization*

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

*Opinion*

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

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

*Intended Users and Purpose*

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

[Service auditor's signature]

[Date of the service auditor's assurance report]

[Service auditor's address]

### **Example Modified Service Auditor's Assurance Report**

The following examples of modified service auditor's assurance reports are for guidance only and are not intended to be exhaustive or applicable to all situations.

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

“ ...

##### *Service Auditor's Responsibilities*

...

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

##### *Basis for Qualified Opinion*

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

##### *Qualified Opinion*

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

(a) ...”

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

“ ...

##### *Service Auditor's Responsibilities*

...

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



*Basis for Qualified Opinion*

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

*Qualified Opinion*

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

(a) ...”

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

“...

*Service Auditor's Responsibilities*

...

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

*Basis for Qualified Opinion*

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

*Qualified Opinion*

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

(a) ...”

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

“...

*Service Auditor’s Responsibilities*

...

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

*Basis for Qualified Opinion*

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

*Qualified Opinion*

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

(a) ...”

*DRAFTING NOTE TO IAASB: Changes to conforming amendments since the previous version are shown in highlights, rather than revision marks*

## **PROPOSED CONFORMING AMENDMENTS**

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

#### **Other International Standards**

24-1. Some International Standards identified in paragraphs 5-7 contain: objectives, requirements, application and other explanatory material, and introductory material and definitions. These terms are to be interpreted in a directly analogous way to how they are explained in the context of ISAs and financial statement audits in paragraphs 15-22.

24-2. The Other International Standards identified in paragraphs 5-7 contain basic principles and essential procedures ...

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