

ASAE 3500
(July 2008)

**Standard on Assurance
Engagements ASAE 3500**
Performance Engagements

Issued by the **Auditing and Assurance Standards Board**



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PREFACE

Reasons for Issuing Standard on Assurance Engagements ASAE 3500 Performance Engagements

The AUASB makes Auditing Standards under section 336 of the *Corporations Act 2001* for the purposes of the corporations legislation and formulates auditing and assurance standards for other purposes.

The AUASB issues Standard on Assurance Engagements ASAE 3500 *Performance Engagements* pursuant to the requirements of the legislative provisions explained below.

The *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (the CLERP 9 Act) established the AUASB as an independent statutory body under section 227A of the *Australian Securities and Investments Commission Act 2001* (ASIC Act), as from 1 July 2004. Under section 227B of the ASIC Act, the AUASB may formulate Assurance Standards for purposes other than the corporations legislation.

Following the issuance of the *Framework for Assurance Engagements* (Framework) and ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, the AUASB reviewed existing assurance standards issued by the former Auditing & Assurance Standards Board of the Australian Accounting Research Foundation, including AUS 806 *Performance Auditing* (July 2002) and AUS 808 *Planning Performance Audits* (October 1995), and identified the need to update these standards.

Main Features

This Standard on Assurance Engagements (ASAE) establishes mandatory requirements and provides explanatory guidance for conducting and reporting on performance engagements.

Operative Date

This ASAE is operative for performance engagements commencing on or after 1 January 2009.

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AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) formulates this Standard on Assurance Engagements ASAE 3500 *Performance Engagements* as set out in paragraphs 1 to 94, pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*.

This Standard on Assurance Engagements is to be read in conjunction with the *Preamble to AUASB Standards*, which sets out the intentions of the AUASB on how the Standards on Assurance Engagements are to be understood, interpreted and applied.

The mandatory requirements of this Standard on Assurance Engagements are set out in **bold-type** paragraphs.

Dated 31 July 2008

M H Kelsall
Chairman - AUASB

STANDARD ON ASSURANCE ENGAGEMENTS ASAE 3500

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Application

- 1 **This Standard on Assurance Engagements (ASAE) applies to performance engagements which may be a performance audit or a performance review engagement.**

Operative Date

- 2 **This ASAE is operative for performance engagements commencing on or after 1 January 2009.**

Introduction

- 3 The purpose of this ASAE, in addition to the mandatory requirements and explanatory guidance for assurance engagements provided by ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, is to establish mandatory requirements and to provide explanatory guidance for undertaking and reporting on performance engagements. This ASAE applies to assurance practitioners conducting performance engagements.
- 4 The terms “performance audit engagement” and “performance review engagement” distinguish between the two types of performance engagements that an assurance practitioner may conduct under this ASAE. A performance audit engagement provides reasonable assurance, whereas a performance review engagement provides limited assurance.
- 5 A performance engagement with multiple objectives and sub-objectives, which incorporates either or both levels of assurance in the same engagement, may also be conducted under this ASAE. In these circumstances, the activity on which a performance audit is conducted needs to be clearly distinguished from the activity on which a performance review is conducted.

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- 6 The essential elements of performance engagements are:
- (a) a three party relationship involving an assurance practitioner, a responsible party or a number of responsible parties, and intended users, where either the responsible party or the intended user may also be the engaging party;
 - (b) an appropriate activity;
 - (c) suitable criteria;
 - (d) sufficient appropriate evidence; and
 - (e) a written assurance report in a form appropriate to a performance audit engagement or a performance review engagement or a report addressing both levels of assurance.
- 7 The responsible party and the intended users may be from different entities or the same entity. The relationship between the responsible party and the intended users needs to be viewed within the context of a specific performance engagement and may differ from more traditionally defined lines of responsibility. For example, an entity's senior management (the intended user) may engage an assurance practitioner to conduct a performance engagement of a particular aspect of the entity's activities that is the immediate responsibility of a lower level of management (the responsible party), but for which senior management is ultimately responsible. In the public sector, performance engagements may be conducted by an Auditor-General (the assurance practitioner) pursuant to a legislative mandate on a government agency or agencies (the responsible party or parties) for the purpose of reporting to the Parliament (the intended user).

Relationship with Other ASAEs, ASAs and ASREs

- 8 The assurance practitioner shall comply with this ASAE, ASAE 3000 and other applicable ASAEs when conducting a performance engagement of an entity or selected activity of an entity, or a selected activity across a number of entities.**
- 9 ASAE 3000 has been written for general application to assurance engagements other than audits or reviews of historical financial information covered by ASAs or ASREs. Other ASAEs may relate to topics that apply to all subject matters or be subject matter specific. This ASAE has been written for specific application to performance engagements as an adjunct standard to ASAE 3000.

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- 10 In circumstances when a performance engagement includes a compliance component, in accordance with paragraph 8 of this ASAE, the assurance practitioner needs to apply both ASAE 3100 and ASAE 3500 as applicable, as well as ASAE 3000, in conducting the assurance engagement. However, if there is any inconsistency, ASAE 3500 applies.

Inability to Comply with Mandatory Requirements

- 11 Where in rare and exceptional circumstances, factors outside the assurance practitioner's control prevent the assurance practitioner from complying with a relevant mandatory requirement in this ASAE and/or ASAE 3000, the assurance practitioner shall:**
- (a) if possible, undertake appropriate alternative evidence-gathering procedures; and**
 - (b) document in the working papers:**
 - (i) the circumstances surrounding the inability to comply;**
 - (ii) the reasons for the inability to comply; and**
 - (iii) justification of how alternative evidence-gathering procedures achieve the objectives of the mandatory requirement.**

When the assurance practitioner is unable to undertake appropriate alternative evidence-gathering procedures, the assurance practitioner shall assess the implications for the assurance report.

Objective of a Performance Engagement

- 12 The objective of a performance engagement is to enable the assurance practitioner to express a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party by reporting on assertions, or information obtained directly, concerning the economy, efficiency or effectiveness of an activity against identified criteria.**
- 13 In expressing a conclusion, under paragraph 12 of this ASAE, the assurance practitioner uses professional judgement to assess the

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performance of an activity against the identified criteria and whether:

- (a) performance is within the tolerances of materiality (that is, the activity has been carried out economically, efficiently or effectively); or
- (b) performance is outside the tolerances of materiality (that is, the activity has not been carried out economically, efficiently or effectively).

14 While legislation, regulations, predetermined policies or custom may establish the responsible party's responsibility, it may not necessarily be described using the terms economy, efficiency and effectiveness. In these circumstances, the assurance practitioner exercises professional judgement in determining the use of the most appropriate terminology throughout the performance engagement and especially in the assurance report. In conducting a performance engagement, the assurance practitioner is not limited to only using the terms economy, efficiency and effectiveness.

15 Ordinarily, performance engagements address a range of activities including:

- Systems for planning, budgeting, authorisation, control and evaluation of resource allocation.
- Systems established and maintained to ensure compliance with an entity's mandate as expressed in policies or legislation.
- Appropriateness of resource management.
- Measures aimed at deriving economies of scale, such as centralised resource acquisition, sharing common resources across a number of business units.
- Measures aimed at improving economy, efficiency or effectiveness.
- Appropriateness of the assignment of responsibilities, and accountability.
- Measures to monitor outcomes against predetermined objectives and performance benchmarks.

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- 16 In the public sector, the conduct of performance engagements by Auditors-General is legislated in the respective jurisdictions. While the legislative requirements may have either a narrow or broad scope, ordinarily performance engagements include examination of:
- Economy, efficiency or effectiveness:
 - ◆ in terms of management systems or an entity’s management in order to contribute to improvements;
 - ◆ of the operations of an entity or an activity of an entity;
 - ◆ of the internal controls applied by an entity in relation to an activity;
 - ◆ in the implementation of government policies or programs and the application of government grants;
 - ◆ in terms of financial prudence in the application of public resources; and
 - ◆ of administrative arrangements.
 - The validity and reliability of performance measurement systems and/or statements published by the responsible party in annual reports.
 - Compliance with legislation and accompanying instruments and identification of breaches.
 - Intended and unintended impacts of the implementation of government policies or programs and the extent to which community needs and stated objectives of an activity or entity have been met.
 - Probity processes and identification of weaknesses.

Definitions

- 17 In this ASAE, the following terms have the meanings attributed below:
- (a) “Activity” means an action or actions associated with a function or program, including administrative and internal

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control functions, that are integral to the operations of a business unit or an entity. In the context of this ASAE the economy, efficiency or effectiveness of the activity is the subject matter of a performance engagement.

- (b) “Assertion-based Engagement” in the context of a performance engagement means a performance engagement where the assurance practitioner reports on assertions prepared by the responsible party regarding the economy, efficiency or effectiveness of the activity.
- (c) “Assurance practitioner” means a person or an organisation, whether in public practice, industry, commerce or the public sector, involved in the provision of assurance services.
- (d) “Criteria” in the context of a performance engagement means reasonable and acceptable standards of performance against which the extent of economy, efficiency or effectiveness of an activity may be assessed.

Suitable criteria have the following characteristics:

- (i) *relevance*: relevant criteria contribute to conclusions that assist decision-making by the intended users;
- (ii) *completeness*: criteria are sufficiently complete when relevant factors that could affect the conclusions in the context of the performance engagement circumstances are not omitted. Complete criteria include, where relevant, benchmarks for presentation and disclosure;
- (iii) *reliability*: reliable criteria allow reasonably consistent evaluation or measurement of the activity, including when used in similar circumstances by similarly qualified assurance practitioners;
- (iv) *neutrality*: neutral criteria contribute to conclusions that are free from bias; and
- (v) *understandability*: understandable criteria contribute to conclusions that are clear, comprehensive, and not subject to significantly different interpretations.

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- (e) “Direct Reporting Engagement” means performance engagements where the assurance practitioner directly undertakes the evaluation or measurement of the activity to report on the economy, efficiency or effectiveness of the activity.
- (f) “Intended users” means the person, persons or class of persons for whom the assurance practitioner prepares the assurance report. The responsible party can be one of the intended users, but not the sole user.
- (g) “Materiality” in the context of a performance engagement means variations of the measure or assertions from identified criteria for the evaluation or measurement of performance of the activity which, if omitted, misstated or not disclosed has the potential to adversely affect decisions about the economy, efficiency or effectiveness made by users or the discharge of accountability by the responsible party or the governing body of the entity.
- (h) “Performance engagement” means a performance audit or a performance review of all or a part of the activities of an entity (or entities) to assess economy, efficiency or effectiveness. It includes a “performance audit engagement” or a “performance review engagement” directed to assess:
 - (i) the adequacy of an internal control structure or specific internal controls, in particular those intended to safeguard assets and to ensure due regard for economy, efficiency or effectiveness;
 - (ii) the extent to which resources have been managed economically or efficiently; and
 - (iii) the extent to which activities have been effective.

Using identified criteria to evaluate or measure the economy, efficiency or effectiveness of an activity results in assertions or information concerning the performance of that activity. The assurance practitioner gathers sufficient appropriate evidence about these assertions or information to provide a basis for expressing a conclusion in an assurance report. For example, a performance engagement may be directed at management’s assertions or information concerning the effectiveness of an entity’s road

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maintenance program (activity) in reducing traffic accidents as measured against identified criteria.

The terms “performance audit” and “performance review” are predominantly applied in the public sector. In the private sector these audits and reviews are commonly referred to as “operational audits” and “operational reviews”.

- (i) “Performance audit engagement” means a performance engagement where the assurance practitioner provides reasonable assurance. This is where the assurance practitioner’s objective is a reduction in performance engagement risk to an acceptably low level in the circumstances of the performance engagement as the basis for a positive form of expression of the assurance practitioner’s conclusion. Reasonable assurance means a high, but not absolute, level of assurance.
- (j) “Performance review engagement” means a performance engagement where the assurance practitioner provides limited assurance. In a limited assurance engagement the assurance practitioner’s objective is a reduction in performance engagement risk to a level that is acceptable in the circumstances of the assurance engagement, as the basis for a negative form of expression of the assurance practitioner’s conclusion. The acceptable performance engagement risk in a limited assurance engagement is greater than for a reasonable assurance engagement.
- (k) “Performance engagement risk” means the risk that the assurance practitioner expresses an inappropriate conclusion when the performance of an activity is not materially economic, efficient or effective. This would arise where the assurance practitioner draws conclusions based on evidence that is not soundly based or that is improper or incomplete as a result of inadequacies in the evidence gathering process, misrepresentation or fraud.
- (l) “Professional scepticism” means where the assurance practitioner makes a critical assessment, with a questioning mind, of the validity of evidence obtained and is alert to evidence that contradicts or brings into question the reliability of documents and responses to enquiries and other information obtained from management and the responsible party.

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- (m) “Responsible Party” means the person (or persons) who:
 - (i) in a direct reporting engagement, is responsible for the activity; and
 - (ii) in an assertion-based engagement, is responsible for the assertions or information concerning the performance of the activity and may also be responsible for the activity itself. An example of when the responsible party is responsible for the assertions or information concerning the performance of an activity but not responsible for the activity itself is when a central government agency, such as a Treasury or Department of Finance, prepares assertions or information concerning the performance of activities conducted by other government departments.
- 18 In addition to the definitions included at paragraph 17 of this ASAE, the following definitions have the meanings attributed below. These definitions may have broader application in the public sector and should not be seen as limiting existing legislative arrangements or custom.
- (a) “Economy” means the acquisition of the appropriate quality and quantity of resources at the appropriate times and at the lowest cost.
 - (b) “Efficiency” means the use of resources such that output is optimised for any given set of resource inputs, or input is minimised for any given quantity and quality of output.
 - (c) “Effectiveness” means the achievement of the objectives or other intended effects of activities at a program or entity level.

General Principles of a Performance Engagement

Ethical Requirements

- 19 The assurance practitioner shall comply with the fundamental ethical principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.**

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- 20 The concept of independence is fundamental to the assurance practitioner's compliance with the principles of integrity and objectivity under paragraph 19 of this ASAE.
- 21 The applicable code of ethics of a professional accounting body¹ provides a framework of principles that members of assurance teams, firms and network firms use to identify threats to independence, evaluate the significance of those threats and, if the threats are other than clearly insignificant:
- (a) identify and apply safeguards to eliminate the threats; or
 - (b) reduce them to an acceptable level,
- such that independence of mind and independence in appearance are not compromised.
- 22 Where the practitioner is not able to comply with the fundamental ethical principles, including those relating to independence, the practitioner can not claim compliance with this ASAE. In such circumstances, ASAE 3500 may still provide useful guidance.

Quality Control

- 23 The assurance practitioner shall implement procedures to address the following elements of a quality control system that apply to the individual performance engagement:**
- (a) leadership responsibilities for quality on the performance engagement;**
 - (b) ethical requirements;**
 - (c) acceptance of client relationships and specific performance engagements;**
 - (d) assignment of performance engagement teams;**
 - (e) conduct of the performance engagement; and**
 - (f) monitoring.**

¹ The applicable code of ethics of the professional accounting bodies in Australia is *APES 110 Code of Ethics for Professional Accountants*, as issued from time to time by the Accounting Professional and Ethical Standards Board. This code of ethics has been adopted by CPA Australia, National Institute of Accountants, and The Institute of Chartered Accountants in Australia. In addition, codes of ethics issued by other professional bodies may apply.

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- 24 For further guidance on quality control refer to ASAE 3000.
- 25 Depending on the nature of the performance engagement, the assurance practitioner may need to either assemble a multi-disciplinary team or be a specialist in the relevant discipline. A multi-disciplinary team may include expertise in, for example, accounting, economics, legal, organisational psychology, political science and sociology.
- 26 When multi-disciplinary teams are used in a performance engagement, adequate direction, supervision and review are particularly important so that the team members' different perspectives, experience and specialties are appropriately used. It is important that all team members understand the objectives of the particular performance engagement and the terms of reference of work assigned to them. Adequate direction, supervision and review are important so that the work of all team members is executed properly and is in compliance with this ASAE and ASAE 3000.

Performance Engagement Initiation or Acceptance

- 27 The assurance practitioner shall initiate or accept a performance engagement only if:**
- (a) the activity is the responsibility of a party who is not the sole intended user or the assurance practitioner;**
 - (b) on the basis of a preliminary knowledge of the performance engagement circumstances, the assurance practitioner forms the view that:**
 - (i) the requirements of the fundamental ethical principles will be satisfied;**
 - (ii) the activity is appropriate as a subject matter for the performance engagement in that it is identifiable, its performance is capable of consistent measurement against identified criteria or assertions, or information about it is capable of being subjected to procedures for gathering sufficient appropriate evidence;**
 - (iii) the identified criteria are suitable; and**
 - (iv) the requirements of this ASAE or ASAE 3000 will be satisfied; and**

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- (c) **the assurance practitioner is satisfied that those persons who are to conduct the performance engagement collectively possess the necessary professional and technical competencies.**

Communicating or Agreeing on the Terms of the Performance Engagement

- 28 The assurance practitioner shall communicate or agree on the terms of the performance engagement with the engaging party, which shall be recorded in writing by the assurance practitioner and forwarded to the engaging party. When the terms of a performance engagement are changed, the assurance practitioner shall communicate or agree the new terms with the engaging party in writing. When the performance engagement is undertaken or changed pursuant to legislation, the applicable performance engagement terms shall be those contained in the legislation.**
- 29 To avoid misunderstandings, under paragraph 28 of this ASAE, the agreed terms of the performance engagement need to be recorded in a performance engagement letter or other suitable form of contract. If the engaging party is not the responsible party, the nature and content of a performance engagement letter or contract may be different from when the engaging party is the responsible party. The existence of a legislative mandate may satisfy the requirement to agree on the terms of the performance engagement. Even in those situations an assurance engagement letter may be useful for both the assurance practitioner and engaging party.
- 30 Where there is a legislated mandate that gives an assurance practitioner the discretion to determine or change the terms of the performance engagement, the assurance practitioner's notification of the legislative mandate and focus of the proposed performance engagement to the responsible party satisfies the requirements under paragraph 28 of this ASAE.
- 31 A change in circumstances that affects the intended users' needs, or a misunderstanding concerning the nature of the performance engagement, ordinarily may justify a change in the terms of the performance engagement. If such a change is made, the assurance practitioner does not disregard evidence that was obtained prior to the change.

Planning and Conducting the Performance Engagement

- 32 **The assurance practitioner shall plan a performance engagement so that it will be conducted effectively and achieves the objectives communicated or agreed in the terms of the performance engagement.**
- 33 Planning involves developing an overall strategy for the scope, emphasis, timing and conduct of the performance engagement, and a performance engagement plan, consisting of a detailed approach for the nature, timing and extent of evidence-gathering procedures to be undertaken and the reasons for selecting them. Ordinarily, adequate planning:
- Helps to devote appropriate attention to important areas of the performance engagement, identify potential problems on a timely basis and properly organise and manage the performance engagement in order for it to be conducted in an effective and efficient manner.
 - Assists the assurance practitioner to properly assign work to performance engagement team members, and facilitates their direction and supervision and the review of their work.
 - Assists, where applicable, the coordination of work done by other assurance practitioners and experts.
- 34 The nature and extent of planning activities will vary with the performance engagement circumstances, for example the size and complexity of the activity and the assurance practitioner's previous experience with it. Examples of the main matters to be considered include:
- The terms of the performance engagement.
 - The characteristics of the activity and the identified criteria.
 - The performance engagement process and possible sources of evidence.
 - The assurance practitioner's understanding of the activity and other performance engagement circumstances.
 - Identification of intended users and their needs, and consideration of materiality and the components of performance engagement risk.

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- Personnel and expertise requirements, including the nature and extent of involvement by experts.
- 35 Planning is not a discrete phase, but rather a continual and iterative process throughout the performance engagement. As a result of unexpected events, changes in conditions, or the evidence obtained from the results of evidence-gathering procedures, the assurance practitioner may need to revise the overall strategy and performance engagement plan, and thereby the resulting planned nature, timing and extent of further evidence-gathering procedures.
- 36 The assurance practitioner shall plan and conduct a performance engagement with an attitude of professional scepticism recognising that circumstances may exist that cause the:**
- (a) **activity not to be economic, efficient or effective; and/or**
 - (b) **assertions or information concerning the activity to be materially misstated.**

Understanding the Activity

- 37 The assurance practitioner shall obtain an understanding of the activity and other performance engagement circumstances sufficient to identify and assess the performance engagement risks of the activity not being economic, efficient or effective, and sufficient to design and undertake further evidence-gathering procedures.**
- 38 Obtaining an understanding of the activity and other performance engagement circumstances is an essential part of planning and conducting a performance engagement. That understanding ordinarily provides the assurance practitioner with a frame of reference for exercising professional judgement throughout the performance engagement, for example, when:
- Considering the characteristics of the activity.
 - Assessing the suitability of criteria.
 - Assessing systems established and maintained for ensuring compliance with an entity's mandate or internal controls as expressed in policies and legislation.

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- Identifying where special consideration may be necessary, for example factors indicative of wastage or fraud, and the need for specialised skills or the work of an expert.
- Establishing and evaluating the continued appropriateness of quantitative levels of performance (where appropriate), and considering qualitative materiality factors or benchmarks.
- Developing expectations for use when undertaking analytical procedures.
- Designing and undertaking further evidence-gathering procedures to reduce performance engagement risk to an appropriate level.
- Evaluating evidence, including the reasonableness of the responsible party's oral and written representations.

39 The assurance practitioner uses professional judgement to determine the extent of the understanding that is needed of the activity and other performance engagement circumstances. Under paragraph 37 of this ASAE, the assurance practitioner needs to consider whether the understanding is sufficient to assess the performance engagement risk that the activity may not be materially economic, efficient or effective or information asserted about the activity is materially misstated. The assurance practitioner ordinarily has a lesser depth of understanding than the responsible party.

Assessing the Appropriateness of the Activity as the Subject Matter

40 The assurance practitioner shall assess the appropriateness of the activity as the subject matter, in terms of:

- (a) being identifiable, and its performance capable of consistent assessment against identified criteria; and**
- (b) ensuring the information about it is capable of being subjected to procedures for gathering sufficient appropriate evidence to support a reasonable assurance or limited assurance conclusion, as appropriate.**

41 The assurance practitioner also ordinarily identifies those characteristics of the activity that are particularly relevant to the intended users, which are to be described in the assurance report. As indicated in paragraph 27(b) of this ASAE, an assurance practitioner does not initiate or accept a performance engagement unless the

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assurance practitioner's preliminary knowledge of the performance engagement circumstances indicates the appropriateness of the activity as the subject matter prior to commencing the engagement.

42 If after initiating or accepting the performance engagement, the assurance practitioner concludes that the activity is not a subject matter appropriate to being subjected to audit or review, the assurance practitioner shall assess whether to:

- (a) change the terms of the performance engagement as described in paragraph 28 of this ASAE; or**
- (b) withdraw from or discontinue the performance engagement.**

43 In the event that the assurance practitioner is unable to change the terms of, or withdraw from or discontinue, the performance engagement, under paragraph 89(c) of this ASAE, the assurance practitioner needs to consider the implications for the assurance report.

Assessing the Suitability of the Criteria

44 The assurance practitioner shall assess the suitability of the criteria to evaluate or measure the performance of the activity.

45 Criteria may range from general to specific. General criteria are broad statements of acceptable and reasonable performance. Specific criteria are derived from general criteria and are more closely related to an entity's governing legislation or mandate, objectives, programs, systems and controls. The level of detail of the assurance practitioner's conclusions is affected by the level of detail at which the criteria are specified.

46 Suitable criteria may be derived from sources such as:

- Regulatory bodies, legislation or policy statements.
- Standards of good practice developed by professions, associations or other recognised authorities.
- Statistics or practices developed within the entity or among similar entities.
- Criteria identified in similar circumstances.

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- 47 As indicated in paragraph 27(b) of this ASAE, an assurance practitioner does not initiate or accept a performance engagement unless the assurance practitioner's preliminary knowledge of the performance engagement circumstances indicates that the identified criteria are suitable.
- 48 **If after initiating or accepting the performance engagement, the assurance practitioner concludes that the identified criteria are not suitable, the assurance practitioner shall assess whether to:**
- (a) **change the terms of the performance engagement as described in paragraph 28 of this ASAE; or**
 - (b) **withdraw from or discontinue the performance engagement.**
- 49 In the event that the assurance practitioner is unable to change the terms of, or withdraw from or discontinue, the performance engagement, under paragraph 89(c) of this ASAE, the assurance practitioner needs to consider the implications for the assurance report.
- 50 Criteria are either established or specifically developed. Ordinarily, established criteria are suitable when they are relevant to the needs of the intended users. When established criteria exist for an activity, specific users may agree to other criteria for their specific purposes. For example, various frameworks can be used as established criteria for evaluating the effectiveness of internal control. Specific users may, however, develop a more detailed set of criteria that meet their specific needs in relation to, for example, program administration where the assurance report may state:
- (a) when it is relevant to the circumstances of the performance engagement, that the criteria are not embodied in laws or regulations, or issued by authorised or recognised bodies of experts that follow a transparent due process; and
 - (b) that it is only for the use of the specific users and for their purposes.
- 51 For some activities it is likely that no established criteria exist. In those cases, criteria are specifically developed. Ordinarily, the assurance practitioner:
- Considers whether specifically developed criteria result in an assurance report that is misleading to the intended users.

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- Attempts to have the intended users or the responsible party acknowledge that specifically developed criteria are suitable for the intended users' purposes.
- Considers how the absence of such an acknowledgement affects what is to be done to assess the suitability of the identified criteria, and the information provided about the criteria in the assurance report.

52 The assurance practitioner may use criteria developed by the responsible party for evaluating or measuring an activity if, in the assurance practitioner's opinion, they are suitable. The responsible party may have developed a system of performance assessment and monitoring incorporating the use of internally developed criteria. In assertion-based engagements, this system of performance assessment may form the basis of the responsible party's written assertions regarding economy, efficiency or effectiveness of an activity.

Materiality and Performance Engagement Risk

53 The assurance practitioner shall consider materiality and performance engagement risk when planning and conducting a performance engagement.

54 Under paragraph 53 of this ASAE, the assurance practitioner needs to consider materiality and performance engagement risk together when:

- (a) determining the nature, timing and extent of evidence-gathering procedures; and
- (b) evaluating whether the assertion or information concerning the economy, efficiency or effectiveness of the activity is free of misstatement.

In considering materiality the assurance practitioner needs to understand and assess what deficiencies in systems and controls or variations from the identified criteria might influence the decisions of the intended users. For example, in an assertion-based engagement, when the identified criteria allow for variations in the presentation of the information about the economy, efficiency or effectiveness of the activity, the assurance practitioner ordinarily considers how the adopted presentation might influence the decisions of the intended users.

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- 55 Ordinarily, the assurance practitioner plans to examine material areas where the performance engagement risk is assessed to be high as well as material areas where the performance engagement risk is assessed as low but where any significant variation from or deficiency, when evaluated or measured against identified criteria in that area, could have a material effect on decisions about the economy, efficiency or effectiveness of the activity.
- 56 Materiality is considered in the context of quantitative and qualitative factors, such as relative magnitude, the nature and extent of the effect of these factors on the evaluation or measurement of the activity and the interests of the intended users. The assessment of materiality and the relative importance of quantitative and qualitative factors in a particular performance engagement are matters for the assurance practitioner's judgement.
- 57 Ordinarily, the assurance practitioner considers quantitative and qualitative factors when assessing materiality and performance engagement risk. These factors include:
- The importance of the activity to achieving the entity's objectives.
 - The financial impact the activity has on the entity as a whole.
 - The nature of transactions, for example, high volumes, large dollar values and complex transactions.
 - The extent of interest shown in particular aspects of the activity by, for example, the legislature or other governing body, regulatory authorities or the public.
 - The economic, social, political and environmental impact of the activity.
 - The extent of management's actions regarding issues raised in previous performance engagements.
 - The diversity, consistency and clarity of the entity's objectives and goals.
 - The nature, size and complexity of the activity.
 - The complexity and quality of management information and external reporting.

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- The effectiveness of internal control, including the level of coverage by the internal auditors.
- The nature and degree of change in the environment or within the entity that impact on the activity.
- Management's effectiveness in a particular area.

58 The assurance practitioner shall reduce performance engagement risk to an acceptable level in the circumstances of the performance engagement.

59 In a performance audit engagement, under paragraph 58 of this ASAE, the assurance practitioner needs to reduce performance engagement risk to an acceptably low level in the circumstances of the performance engagement to obtain reasonable assurance as the basis for a positive form of expression of the assurance practitioner's conclusion.

60 In a performance review engagement, the combination of the nature, timing, and extent of evidence-gathering procedures is at least sufficient to reduce performance engagement risk to a level that is acceptable in the circumstances of the assurance engagement, but where that risk is greater than that for a reasonable assurance engagement, as the basis for a negative form of expression of the assurance practitioner's conclusion.

Using the Work of an Expert

61 When using the work of an expert in the performance engagement, the assurance practitioner shall collect and evaluate evidence in accordance with ASAE 3000.

Obtaining Evidence

62 The assurance practitioner shall obtain sufficient appropriate evidence on which to base the assurance practitioner's conclusions.

63 Sufficiency is the measure of the quantity of evidence. Appropriateness is the measure of the quality of evidence; that is, its relevance and its reliability. The assurance practitioner ordinarily considers the relationship between the cost of obtaining evidence and the usefulness of the information obtained. However, the matter of difficulty or expense involved is not in itself a valid basis for omitting an evidence-gathering procedure for which there is no

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alternative. The assurance practitioner uses professional judgement and exercises professional scepticism in evaluating the quantity and quality of evidence, and thus its sufficiency and appropriateness, to support the conclusions in the assurance report.

- 64 Performance audit and performance review engagements both require the application of assurance skills and techniques and the gathering of sufficient appropriate evidence as part of an iterative, systematic assurance engagement process. For further guidance on the nature, timing and extent of evidence-gathering procedures for performance audit and performance review engagements, refer to ASAE 3000.
- 65 For both performance audit and performance review engagements, if the assurance practitioner becomes aware of a matter that leads the assurance practitioner to question whether sufficient appropriate evidence has been obtained, the assurance practitioner ordinarily pursues the matter by undertaking other evidence-gathering procedures sufficient to enable the assurance practitioner to report.

Evaluation and Communication of Deficiencies and Variations

- 66 The assurance practitioner shall evaluate, individually and in aggregate, whether:**
- (a) deficiencies in systems or controls; and/or**
 - (b) variations of the measures or assertions from the identified criteria**
- that have come to the attention of the assurance practitioner are material to the conclusions in the assurance report.**
- 67 Under paragraph 66 of this ASAE, the assurance practitioner needs to exercise professional judgement in evaluating the materiality of deficiencies in systems and controls and variations in economy, efficiency or effectiveness of the activity.
- 68 The assurance practitioner shall make the responsible party aware of:**
- (a) deficiencies in systems and controls; and**
 - (b) variations of the measures or assertions from the identified criteria,**

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that have come to the attention of the assurance practitioner and are material to the conclusions in the assurance report.

- 69 Under paragraph 66 of this ASAE, the assurance practitioner needs to consider the impact of material system or control deficiencies and material variations in the performance of the activity when evaluated or measured against the identified criteria, on the conclusions in the assurance report. A variation or deficiency is material when, in the assurance practitioner's judgement, it has the potential to adversely:
- (a) affect decisions made by intended users about the economy, efficiency or effectiveness of an activity; or
 - (b) the discharge of accountability by the responsible party or the governing party of the entity.

Representations by the Responsible Party

70 The assurance practitioner shall endeavour to obtain written representations from the responsible party, as appropriate for the engagement.

71 When the responsible party's responsibilities are prescribed by law or regulation, the written representations required under paragraph 70 of this ASAE are ordinarily described in the same manner as that prescribed by law or regulation. Ordinarily, in a direct reporting performance engagement, the responsible party may not be in a position to provide representations to the assurance practitioner.

72 In the public sector, written representations may involve the responsible party's comments on the factual accuracy of the assurance practitioner's findings, which form the basis of the assurance practitioner's conclusions and which may be included in the assurance report.

73 Representations by the responsible party cannot replace other evidence the assurance practitioner could reasonably expect to be available. An inability to obtain sufficient appropriate evidence regarding a matter that has, or may have, a material effect on the evaluation or measurement of the activity, when such evidence would ordinarily be available, constitutes a limitation on the scope of the performance engagement, even if a representation from the responsible party has been received on the activity.

Considering Subsequent Events

- 74 The assurance practitioner shall consider the effect on the activity and on the assurance report of events up to the date of the assurance report.**
- 75 The extent of consideration of subsequent events, that come to the attention of the assurance practitioner, depends on the potential for such events to affect the activity and to affect the appropriateness of the assurance practitioner's conclusions. Consideration of subsequent events in some performance engagements may not be relevant because of the nature of the activity.

Documentation

- 76 The assurance practitioner shall prepare, on a timely basis, documentation that is sufficient and appropriate to provide:**
- (a) a basis for the assurance practitioner's conclusion and recommendations; and**
 - (b) evidence that the performance engagement was conducted in accordance with this ASAE and ASAE 3000.**
- 77 Documentation includes a record of the assurance practitioner's reasoning on all significant matters that require the exercise of judgement, and related conclusions. The existence of difficult questions of principle or judgement, calls for the documentation to include the relevant facts that were known by the assurance practitioner at the time the conclusion was reached.
- 78 In applying professional judgement to assessing the extent of documentation to be prepared and retained, the assurance practitioner ordinarily considers what is necessary to provide an understanding of the work undertaken and the basis of the principal decisions taken to another experienced assurance practitioner who has no previous experience with the performance engagement. It is, however, neither necessary nor practicable to document every matter the assurance practitioner considers during the performance engagement.

Preparing the Assurance Report

- 79 The assurance practitioner shall determine whether sufficient appropriate evidence has been obtained to support the conclusions expressed in the assurance report.**
- 80 In circumstances when a performance engagement incorporates both performance audit of an activity and performance review on another activity, under paragraph 79 of this ASAE, the assurance practitioner needs to clearly distinguish the two types of conclusions expressed.
- 81 In developing the conclusion, the assurance practitioner ordinarily considers all relevant evidence obtained, regardless of whether it appears to corroborate or to contradict information about the economy, efficiency or effectiveness of the activity. The assurance practitioner's conclusion in a direct reporting engagement may consist of a series of conclusions about different aspects of a number of activities where this is appropriate in the context of the particular performance engagement.
- 82 The assurance report shall be in writing and shall contain a clear expression of the assurance practitioner's conclusion against the objectives communicated or agreed in the terms of the performance engagement.**

Assurance Report Content

- 83 Other than to the extent that it is inconsistent with relevant legislation or regulation, the assurance report shall include the following basic elements:**
- (a) **a title that clearly indicates the report is an independent assurance report;**
 - (b) **an addressee;**
 - (c) **an identification and description of the activity;**
 - (d) **identification of the criteria;**
 - (e) **where appropriate, a description of any significant, inherent limitation associated with the evaluation or measurement of the activity against the criteria;**

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- (f) **when the criteria used to evaluate or measure the activity are available only to specific intended users, or are relevant only to a specific purpose, a statement restricting the use of the assurance report to those intended users or that purpose;**
- (g) **a statement to identify the responsible party and to describe the responsible party's and the assurance practitioner's responsibilities;**
- (h) **a statement that the performance engagement was conducted in accordance with applicable ASAEs (ASAE 3500 *Performance Engagements*) and the level of assurance provided;**
- (i) **a summary of the work undertaken;**
- (j) **the assurance practitioner's conclusions:**
 - (i) **where appropriate, shall inform the intended users of the context in which the assurance practitioner's conclusions are to be read;**
 - (ii) **shall be expressed in the positive form where reasonable assurance is provided;**
 - (iii) **shall be expressed in the negative form where limited assurance is provided;**
 - (iv) **where both positive and negative forms are expressed, shall clearly separate the two types of conclusions; and**
 - (v) **where the assurance practitioner expresses a conclusion that is other than unqualified, the assurance report shall contain a clear description of the reasons;**
- (k) **the assurance report date; and**
- (l) **the name of the firm or the assurance practitioner, and a specific location, which ordinarily is the city where the assurance practitioner maintains the office that has responsibility for the performance engagement.**

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- 84 This ASAE does not require a standardised format for reporting on all performance engagements even though at paragraph 83 it identifies the basic elements of the assurance report. For instance, under:
- Paragraph 83(a), the title of the assurance report may differ depending on whether the assurance practitioner is an Auditor-General or a practitioner in the private sector. However, in both instances the title would convey that it is an independent report.
 - Paragraph 83(j), the assurance practitioner's conclusions on an activity may include a combination of positive and negative forms which may be inseparable but essential to be reported as such for the purposes of effectively communicating the assurance practitioner's conclusions to the intended users.
 - Paragraph 83(j)(i), the assurance practitioner's conclusions may be drafted as appropriate to recognise local legislation or custom.
- 85 Therefore, assurance reports are tailored to the specific performance engagement circumstances with the assurance practitioner using professional judgement in deciding how best to meet the reporting requirements detailed in paragraph 83 in conveying the conclusion(s). The assurance practitioner may choose a short form or long form style of reporting to facilitate effective communication to the intended users. Short-form reports ordinarily include only the basic elements. Long form reports often describe in detail the terms of the performance engagement, the criteria being used, findings relating to particular aspects of the performance engagement and, in some cases, recommendations, as well as the basic elements. Ordinarily, any findings and recommendations are clearly separated from the assurance practitioner's conclusion on the economy, efficiency or effectiveness of the activity, and the wording used in presenting them makes it clear they are not intended to affect the assurance practitioner's conclusion.

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Reporting Findings, Recommendations and Responsible Party Comments

86 The assurance practitioner may expand the assurance report to include other information and explanations that are not intended to affect the assurance practitioner's conclusion. Examples include:

- Disclosure of materiality levels.
- Findings relating to particular aspects of the performance engagement.
- Recommendations.
- Comments received from the responsible party.

The decision to include any such information depends on its significance to the needs of the intended users. Additional information is clearly separated from the assurance practitioner's conclusion and worded in such a manner so as not to affect that conclusion.

87 Under a direct reporting engagement, the assurance report ordinarily describes relevant facts and findings to allow intended users to understand the basis upon which the assurance practitioner's conclusions and recommendations have been formed. Findings arise from an examination of the underlying facts, comparison with identified criteria and the assurance practitioner's analysis of the variations in the performance of the activity against criteria, including, where applicable, the causes and effects of the variations.

Modifications to the Assurance Report

88 Modifications to the assurance report relate to circumstances when the assurance practitioner is unable to express an unqualified conclusion and an assurance report is issued with either:

- (a) a qualified conclusion;
- (b) an adverse conclusion; or
- (c) a disclaimer of conclusion.

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Qualified Conclusions, Adverse Conclusions and Disclaimers of Conclusion

- 89** **The assurance practitioner shall not express an unqualified conclusion when the following circumstances exist and, in the assurance practitioner’s judgement, the effect of the matter is or may be material:**
- (a) there is a limitation on the scope of the assurance practitioner’s work, that is, circumstances prevent, or the responsible party or the engaging party imposes a restriction that prevents the assurance practitioner from obtaining evidence required to reduce performance engagement risk to the appropriate level. The assurance practitioner shall express a qualified conclusion or a disclaimer of conclusion; or**
 - (b) in those cases where:**
 - (i) the assurance practitioner’s conclusion is worded in terms of the responsible party’s assertion, and that assertion is not fairly stated in all material respects; or**
 - (ii) the assurance practitioner’s conclusion is worded directly in terms of the activity and the performance against identified criteria is not materially economic, efficient or effective,**

the assurance practitioner shall express a qualified conclusion or adverse conclusion.
 - (c) in the case of an assertion-based engagement when it is discovered, after the engagement has been initiated or accepted, that the activity is not a subject matter appropriate to being subjected to audit or review, or the identified criteria are not suitable, the assurance practitioner shall express:**
 - (i) a qualified or adverse conclusion when the unsuitable criteria or inappropriate subject matter is likely to mislead the intended users; or**
 - (ii) a qualified conclusion or a disclaimer of conclusion in other cases.**

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- 90** The assurance practitioner shall express a qualified conclusion when the effect of a matter is not so material or pervasive as to require an adverse conclusion or a disclaimer of conclusion. A qualified conclusion is expressed as being “except for” or otherwise discloses the effects of the matter to which the qualification relates.

Other Reporting Responsibilities

- 91** In addition to communicating material deficiencies and variations, as required by paragraph 68 of this ASAE, the assurance practitioner shall consider other reporting responsibilities, including the appropriateness of communicating relevant matters of governance interest arising from the performance engagement with the responsible party.
- 92 Relevant matters of governance interest include only those matters that have come to the attention of the assurance practitioner while conducting the performance engagement. If the terms of the performance engagement do not specifically require it, the assurance practitioner is not required to design procedures for the specific purpose of identifying matters of governance interest.
- 93** The assurance practitioner shall consider any other reporting responsibilities set by legislation.

Conformity with International Standards on Assurance Engagements

- 94 There is no corresponding International Standard on Assurance Engagements.