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Prof Roger Simnett
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Dear Roger

ED 01/17 Proposed Standard on Assurance Engagements ASAE 3500 *Performance Engagements*

CPA Australia welcomes the opportunity to respond to ED 01/17. We make this submission on behalf of our members and in the broader public interest.

We consider that ASAE 3500 is an important standard in promoting a consistent approach to performance engagements across Australia. We welcome the revision of the standard and support it, as the requirements and application material provide greater clarity on how to conduct performance engagements in a manner that reflects the approach in ASAE 3000. Whilst the proposed standard is sound, there are some aspects that would benefit from amendment, as set out in answer to the specific questions below.

1. Have applicable laws and regulations been appropriately addressed in the proposed standard?

We have not identified any concerns regarding addressing applicable laws and regulations.

2. Are there any references to relevant laws or regulations that have been omitted?

We are not aware of any omissions.

3. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

We are not aware of any laws or regulations which prevent, impede or conflict with the proposed standard.

4. What, if any, are the additional significant costs to/benefits for assurance practitioners and the public sector arising from compliance with the main changes to the requirements of this proposed standard? If there are significant costs, do these outweigh the benefits to the users of performance engagements?

There are likely to be some additional costs in implementing the proposed standard in order to update methodologies for the revised requirements and to ensure that areas which impose more comprehensive requirements are adequately addressed, such as internal controls. We do not consider that those additional costs are likely to be significant, although they will depend on the characteristics of the activity, such as the complexity of the relevant internal controls.

5. Will there be any difficulties in implementing the requirements?

There are several matters which we consider may cause implementation difficulties. We have identified these matters and, where appropriate, we have set out recommendations as to how the standard could be amended to address them.

1. Definition of Materiality – paragraph 17(m)

Materiality is defined in the ED as: ‘variations in performance of an activity against the identified criteria which, if omitted, misstated or not disclosed has the potential to adversely affect decisions about the economy, efficiency and/or effectiveness and be reasonably expected to influence relevant decisions of the intended users or the discharge of accountability by the responsible party or governing body of the entity.’

Performance engagements covered by the proposed standard are direct engagements, which would not usually give rise to an ‘omission, misstatement or non-disclosure’ as the performance would not have been reported on by the entity. In addition, as variations may exceed identified criteria, decisions are not necessarily always ‘adversely’ affected. Furthermore, we suggest that the definition should identify the impact on performance and then whether it affects decisions, rather than referring to decisions twice.

In addition, materiality is considered in the context of planning and in evaluation of findings.

To address these concerns, we recommend that the definition of materiality should be amended as follows:

Variations in performance of an activity evaluated against the identified criteria which, ~~if omitted, misstated or not disclosed has~~ have the potential to ~~adversely affect decisions about~~ the economy, efficiency and/or effectiveness of the activity and be reasonably expected to influence relevant decisions of the intended users or the discharge of accountability by the responsible party or governing body of the entity.

If the definition of materiality is amended, then the wording of paragraphs 32 and A42 may need to be amended to be consistent, by deleting the word ‘adversely’.

2. Definition of Reasonable assurance engagement – paragraph 17(p)

The definition of reasonable assurance engagement and limited assurance engagement should be consistent. In the proposed standard the definition of limited assurance is more specific to performance engagements as it refers to economy, efficiency and effectiveness. We suggest that the definition of reasonable assurance engagements also

needs to be more specific to make it meaningful for performance engagements. Our recommended wording is set out in point 5 below.

3. Definition of Variation – paragraph 17(t)

Variation is defined in the ED as: ‘An instance where the underlying subject matter does not meet in whole or part the identified criteria, for example a material departure of performance against the identified criteria.’

We note that the term ‘variation’ may be useful in the context of performance engagements if it is intended to reflect both deficiencies in performance and positive performance (including outstanding performance or performance exceeding expectations or benchmarks). In contrast, other types of assurance engagements usually seek to identify only negative findings, such as misstatements in reports, deficiencies in the design or implementation of controls, deviations in the operating effectiveness of controls or non-compliance.

However, the definition of variation in the ED arguably reflects only deficiencies in performance as it states: ‘An instance where the underlying subject matter does not meet in whole or part the identified criteria’ (emphasis added). We recommend that either the definition is amended to reflect both positive and negative variations or a term which is more consistent with existing standards, such as ‘deficiencies’, should be used.

Further, we consider that the second half of the definition does not add any clarity and the inclusion of the word ‘material’ is unhelpful as variations may be either material or immaterial. Once a variation is identified, materiality is a separate consideration which will determine whether it will impact the assurance conclusion.

Consequently, we suggest that either the term ‘variation’ is replaced with ‘deficiency’ or, if it is retained, that the definition of variation be amended as follows:

An instance where the performance of the underlying subject matter ~~does not meet either exceeds the identified criteria or is deficient,~~ in whole or part, as evaluated against the identified criteria, ~~for example a material departure of performance against the identified criteria~~

4. Internal controls – paragraph 34

Whilst we support the proposed requirements in relation to internal controls, the nature, timing and extent of testing necessary to evaluate the design and implementation of controls as required under paragraph 34, may create implementation difficulties for some practitioners. The proposed requirements are much more explicit that relevant controls should be considered, but do not specify the procedures required to be conducted. We acknowledge that, as only internal controls ‘relevant to the evaluation of the activity’s performance against the identified criteria’ are required to be understood, it may not be possible to clarify the procedures required, but a list of possible types procedures may be helpful in the application material.

5. Assurance Conclusion – paragraph 42

We consider that the assurance conclusion as described in paragraph 42 could more closely reflect the usual manner in which performance is described. In particular, the phrase ‘free of material variation’ could be replaced with a phrase which more closely aligns with the objective (para. 16) and definition (para. 17(n)) of a performance engagement.

We recommend that the wording should be amended as follows:

Para. 42: The assurance practitioner shall form a conclusion about whether the activity has been performed ~~performance of the activity~~, as evaluated against the identified criteria, ~~is free of material variation~~ economically, efficiently and/or effectively, in all material respects.

This conclusion wording also needs to be reflected consistently in the definitions of limited assurance and reasonable assurance in paragraphs 17(l) and (p) respectively. We recommend that the definitions are amended as follows:

Para. 17(l) Limited assurance engagement—An assurance engagement in which the assurance practitioner reduces engagement risk to a level that is acceptable in the circumstances of the engagement, but where that risk is greater than for a reasonable assurance engagement as the basis for the assurance practitioner's conclusion. The assurance practitioner's conclusion is expressed in a form that conveys whether, based on the procedures performed and evidence obtained a matter(s) has come to the assurance practitioner's attention to cause the assurance practitioner to believe the activity has not been performed ~~with respect to economically, efficiently and/or effectively~~ ness, in all material respects, as evaluated against the identified criteria. The nature...

Para. 17(p) Reasonable assurance engagement—An assurance engagement in which the assurance practitioner reduces engagement risk to an acceptably low level in the circumstances of the engagement as the basis for the assurance practitioner's conclusion. The assurance practitioner's conclusion is expressed in a form that conveys whether in the assurance practitioner's opinion ~~conclusion on the outcome of the evaluation of the activity~~ has been performed economically, efficiently and/or effectively, in all material respects, as evaluated against identified criteria.

In addition, it would be helpful to clarify that this precise wording is not mandatory in the assurance conclusion and the conclusion should reflect the objective of the engagement.

6. Minor amendments

Para. 5: Paragraph 5 is redundant as most of its content is covered in paragraph 3, so we suggest that paragraph 5 is deleted and the additional words in paragraph 5 are added to paragraph 3.

Para. 7(a)(i): As performance engagements can also be conducted in the private sector or outsourced by the Auditors General to the private sector, we recommend amending the wording to read: '..., ~~often~~ including a State, Territory or National Auditor General'.

Para. 17(r): The definition of 'responsible party' would benefit from further clarification by adding the phrase underlined as follows: 'The party responsible for the performance of all or part of the activity, in a-which is the subject matter of the performance engagement.'

Para. A3(f): We suggest that activities specifically include governance structures by inserting the words 'Governance structures, including' in this sub-paragraph before 'the assignment...'.
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6. **Are there any other significant public interest matters that constituents wish to raise?**

We have not identified any other significant public interest issues.

If you require further information on our views expressed in this submission, please contact Claire Grayston on (03) 9606 5183 or at claire.grayston@cpaaustralia.com.au.

Yours sincerely

A handwritten signature in grey ink, consisting of a large, stylized 'S' followed by a horizontal line extending to the right.

Stuart Dignam
General Manager, Policy & Corporate Affairs