

**ASA 210**  
(October 2009)

**Auditing Standard ASA 210**  
*Agreeing the Terms of Audit*  
*Engagements* (**Revised and**  
**Redrafted**)

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

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## PREFACE

### **Reasons for Issuing Auditing Standard ASA 210** ***Agreeing the Terms of Audit Engagements* (Revised and Redrafted)**

The Auditing and Assurance Standards Board (AUASB) issues Auditing Standard ASA 210 *Agreeing the Terms of Audit Engagements* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is an independent statutory board of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Australian Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the International Auditing and Assurance Standards Board (IAASB) for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards. Accordingly, the AUASB has decided to revise and redraft the Australian Auditing Standards using the equivalent redrafted ISAs.

## Main Features

This Auditing Standard establishes ~~mandatory~~ Requirements and provides Application and Other Explanatory Material regarding the auditor's responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance.

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This Auditing Standard:

- (a) requires the auditor to establish that the preconditions for an audit are present, including management's use of an acceptable financial reporting framework, and agreement and acknowledgement of its responsibilities in the preparation of the financial report. The auditor must determine that the financial reporting framework is acceptable and obtain the agreement of management that it acknowledges and understands its responsibilities;
- (b) prohibits an auditor from accepting, unless required to by law or regulation, an audit engagement where management has imposed a limitation in scope that the auditor believes will result in a disclaimer of opinion on the financial report;
- (c) requires the auditor to agree the terms of the audit engagement with management or those charged with governance;
- (d) requires the auditor to record the terms of engagement in an audit engagement letter or other suitable form of written agreement;
- (e) describes the requirements when the auditor has to address a change in the terms of an audit engagement; and
- (f) provides direction when:
  - the financial reporting standards are supplemented by law or regulation;
  - the financial reporting framework is prescribed by law or regulation; and
  - the auditor's report is prescribed by law or regulation.

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**~~AUASB Information Note~~**

~~The IAASB has announced completion of the “Clarity” project. While all currently known conforming amendments are incorporated into this Exposure Draft, readers are advised that the AUASB may decide to make further conforming amendments and other editorial changes.~~

### **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 210 *Agreeing the Terms of Audit Engagements* ~~(Revised and Redrafted)~~ pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*.

This Auditing Standard is to be read in conjunction with ASA 101 *Preamble to Australian Auditing Standards* ~~(Revised and Redrafted)~~, which sets out the intentions of the AUASB on how the Australian Auditing Standards, operative for financial reporting periods commencing on or after 1 January 2010, are to be understood, interpreted and applied. *This Auditing Standard is to be read also in conjunction with ASA 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards.*

AUASB

Dated 27 October 2009

M H Kelsall  
Chairman - AUASB

## AUDITING STANDARD ASA 210

### ***Agreeing the Terms of Audit Engagements* (Revised and Redrafted)**

#### **Application**

- Aus 0.1 This Auditing Standard applies to:
- (a) an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
  - (b) an audit of a financial report, or a complete set of financial statements, for any other purpose.
- Aus 0.2 This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

#### **Operative Date**

- Aus 0.3 This Auditing Standard is operative for financial reporting periods commencing on or after 1 January 2010.

#### **Introduction**

##### **Scope of this ASA Auditing Standard**

1. This Auditing Standard deals with the auditor's responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance. This includes establishing that certain preconditions for an audit, responsibility for which rests with management and, where appropriate, those charged with governance, are present. ASA 220 (~~Revised and Redrafted~~)<sup>1</sup> deals with those aspects of engagement acceptance that are within the control of the auditor. (Ref: Para. A1)

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#### **Effective Date**

2. [Deleted by the AUASB. Refer Aus 0.3]

## **Objective**

3. The objective of the auditor is to accept or continue an audit engagement only when the basis upon which it is to be performed has been agreed, through:
- (a) Establishing whether the preconditions for an audit are present; and
  - (b) Confirming that there is a common understanding between the auditor and management and, where appropriate, those charged with governance of the terms of the audit engagement.

## **Definitions**

4. For the purposes of the Australian Auditing Standards, the following terms have the meanings attributed below:

Preconditions for an audit means the use by management of an acceptable financial reporting framework in the preparation of the financial report and the agreement of management and, where appropriate, those charged with governance to the premise<sup>2</sup> on which an audit is conducted.

5. For the purposes of this Auditing Standard, references to “management” should be read hereafter as “management and, where appropriate, those charged with governance.”

## **Requirements**

### **Preconditions for an Audit**

6. In order to establish whether the preconditions for an audit are present, the auditor shall:
- (a) Determine whether the financial reporting framework to be applied in the preparation of the financial report is acceptable; and (Ref: Para. A2-A10)

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<sup>1</sup> See ASA 220 ~~(Revised and Redrafted)~~ *Quality Control for an Audits of a Financial Report and Other Historical Financial Information.*

<sup>2</sup> See ASA 200 ~~(Revised and Redrafted)~~ *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*, paragraph 13.

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(b) Obtain the agreement of management that it acknowledges and understands its responsibility:

(Ref: Para. A11-A14, A20-~~Aus A20.1~~)

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(i) For the preparation of the financial report in accordance with the applicable financial reporting framework, including where relevant their fair presentation; (Ref: Para. A15)

(ii) For such internal control as management determines is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error; and (Ref: Para. A16-A19)

(iii) To provide the auditor with:

- a. Access to all information of which management is aware that is relevant to the preparation of the financial report such as records, documentation and other matters;
- b. Additional information that the auditor may request from management for the purpose of the audit; and
- c. Unrestricted access to persons within the entity from whom the auditor determines it necessary to obtain audit evidence.

*Limitation on Scope Prior to Audit Engagement Acceptance*

7. If management or those charged with governance impose a limitation on the scope of the auditor's work in the terms of a proposed audit engagement such that the auditor believes the limitation will result in the auditor disclaiming an opinion on the financial report, the auditor shall not accept such a limited engagement as an audit engagement, unless required by law or regulation to do so.

*Other Factors Affecting Audit Engagement Acceptance*

8. If the preconditions for an audit are not present, the auditor shall discuss the matter with management. Unless required by law or

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regulation to do so, the auditor shall not accept the proposed audit engagement:

- (a) If the auditor has determined that the financial reporting framework to be applied in the preparation of the financial report is unacceptable, except as provided in paragraph 19; or
- (b) If the agreement referred to in paragraph 6(b) has not been obtained.

**Agreement on Audit Engagement Terms**

- 9. The auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate. (Ref: Para. A21)
- 10. Subject to paragraph 11, the agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include: (Ref: Para. A22-A25)
  - (a) The objective and scope of the audit of the financial report;
  - (b) The responsibilities of the auditor;
  - (c) The responsibilities of management;
  - (d) Identification of the applicable financial reporting framework for the preparation of the financial report; and
  - (e) Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.
- 11. If law or regulation prescribes in sufficient detail the terms of the audit engagement referred to in paragraph 10, the auditor need not record them in a written agreement, except for the fact that such law or regulation applies and that management acknowledges and understands its responsibilities as set out in paragraph 6(b). (Ref: Para. A22, A26-A27)
- 12. If law or regulation prescribes responsibilities of management similar to those described in paragraph 6(b), the auditor may determine that the law or regulation includes responsibilities that, in

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the auditor's judgement, are equivalent in effect to those set out in that paragraph. For such responsibilities that are equivalent, the auditor may use the wording of the law or regulation to describe them in the written agreement. For those responsibilities that are not prescribed by law or regulation such that their effect is equivalent, the written agreement shall use the description in paragraph 6(b).  
(Ref: Para. A26)

#### **Recurring Audits**

13. On recurring audits, the auditor shall assess whether circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the entity of the existing terms of the audit engagement. (Ref: Para. A28)

#### **Acceptance of a Change in the Terms of the Audit Engagement**

14. The auditor shall not agree to a change in the terms of the audit engagement where there is no reasonable justification for doing so. (Ref: Para. A29-A31)
15. If, prior to completing the audit engagement, the auditor is requested to change the audit engagement to an engagement that conveys a lower level of assurance, the auditor shall determine whether there is reasonable justification for doing so. (Ref: Para. A32-A33)
16. If the terms of the audit engagement are changed, the auditor and management shall agree on and record the new terms of the engagement in an engagement letter or other suitable form of written agreement.
17. If the auditor is unable to agree to a change of the terms of the audit engagement and is not permitted by management to continue the original audit engagement, the auditor shall:
  - (a) Withdraw from the audit engagement where possible under applicable law or regulation; and
  - (b) Determine whether there is any obligation, either contractual or otherwise, to report the circumstances to other parties, such as those charged with governance, owners or regulators.

#### **Additional Considerations in Engagement Acceptance**

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*Financial Reporting Standards Supplemented by Law or Regulation*

18. If financial reporting standards established by an authorised or recognised standards setting organisation are supplemented by law or regulation, the auditor shall determine whether there are any conflicts between the financial reporting standards and the additional requirements. If such conflicts exist, the auditor shall discuss with management the nature of the additional requirements and shall agree whether:
- (a) The additional requirements can be met through additional disclosures in the financial report; or
  - (b) The description of the applicable financial reporting framework in the financial report can be amended accordingly.

If neither of the above actions is possible, the auditor shall determine whether it will be necessary to modify the auditor's opinion in accordance with ASA 705 (Revised and Redrafted).<sup>3</sup> (Ref: Para. A34)

*Financial Reporting Framework Prescribed by Law or Regulation—Other Matters Affecting Acceptance*

19. If the auditor has determined that the financial reporting framework prescribed by law or regulation would be unacceptable but for the fact that it is prescribed by law or regulation, the auditor shall accept the audit engagement only if the following conditions are present: (Ref: Para. A35)
- (a) Management agrees to provide additional disclosures in the financial report required to avoid the financial report being misleading; and
  - (b) It is recognised in the terms of the audit engagement that:
    - (i) The auditor's report on the financial report will incorporate an Emphasis of Matter paragraph, drawing users' attention to the additional

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<sup>3</sup> See ASA 705 (Revised and Redrafted) *Modifications to the Opinion in the Independent Auditor's Report*.

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disclosures, in accordance with ASA 706 (Revised and Redrafted);<sup>4</sup> and

- (ii) Unless the auditor is required by law or regulation to express the auditor's opinion on the financial report by using the phrases "present fairly, in all material respects," or "give a true and fair view" in accordance with the applicable financial reporting framework, the auditor's opinion on the financial report will not include such phrases.

20. If the conditions outlined in paragraph 19 are not present and the auditor is required by law or regulation to undertake the audit engagement, the auditor shall:

- (a) Evaluate the effect of the misleading nature of the financial report on the auditor's report; and
- (b) Include appropriate reference to this matter in the terms of the audit engagement.

*Auditor's Report Prescribed by Law or Regulation*

21. In some cases, law or regulation of the relevant jurisdiction prescribes the layout or wording of the auditor's report in a form or in terms that are significantly different from the requirements of the Australian Auditing Standards. In these circumstances, the auditor shall evaluate:

- (a) Whether users might misunderstand the assurance obtained from the audit of the financial report and, if so,
- (b) Whether additional explanation in the auditor's report can mitigate possible misunderstanding.<sup>5</sup>

If the auditor concludes that additional explanation in the auditor's report cannot mitigate possible misunderstanding, the auditor shall not accept the audit engagement, unless required by law or regulation to do so. An audit conducted in accordance with such law or regulation does not comply with Australian Auditing Standards. Accordingly, the auditor shall not include any reference within the

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<sup>4</sup> See ASA 706 (Revised and Redrafted) *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*.

<sup>5</sup> See ASA 706 (Revised and Redrafted).

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auditor's report to the audit having been conducted in accordance with Australian Auditing Standards.<sup>6</sup> (Ref: Para. A36-A37)

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<sup>6</sup> See also ASA 700 ~~(Revised and Redrafted)~~ *Forming an Opinion and Reporting on a Financial Report*, paragraph 43.

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## Application and Other Explanatory Material

### Scope of this ~~ASA Auditing Standard~~ (Ref: Para. 1)

- A1. Assurance engagements, which include audit engagements, may only be accepted when the practitioner considers that relevant ethical requirements such as independence and professional competence will be satisfied, and when the engagement exhibits certain characteristics.<sup>7</sup> The auditor's responsibilities in respect of ethical requirements in the context of the acceptance of an audit engagement and in so far as they are within the control of the auditor are dealt with in ASA 220 (~~Revised and Redrafted~~).<sup>8</sup> This Auditing Standard deals with those matters (or preconditions) that are within the control of the entity and upon which it is necessary for the auditor and the entity's management to agree.

### Preconditions for an Audit

#### *The Financial Reporting Framework* (Ref: Para. 6(a))

- A2. A condition for acceptance of an assurance engagement is that the criteria referred to in the definition of an assurance engagement are suitable and available to intended users.<sup>9</sup> Criteria are the benchmarks used to evaluate or measure the subject matter including, where relevant, benchmarks for presentation and disclosure. Suitable criteria enable reasonably consistent evaluation or measurement of a subject matter within the context of professional judgement. For purposes of the Australian Auditing Standards, the applicable financial reporting framework provides the criteria the auditor uses to audit the financial report, including where relevant its fair presentation.
- A3. Without an acceptable financial reporting framework, management does not have an appropriate basis for the preparation of the financial report and the auditor does not have suitable criteria for auditing the financial report. In many cases, the auditor may presume that the applicable financial reporting framework is acceptable, as described in paragraphs A8-A9.

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<sup>7</sup> See ~~International Framework for Assurance Engagements~~,<sup>2</sup> paragraph 197.

<sup>8</sup> See ASA 220 (~~Revised and Redrafted~~), paragraphs 9-11.

<sup>9</sup> See ~~International Framework for Assurance Engagements~~,<sup>2</sup> paragraph 197(b)(ii).

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Determining the Acceptability of the Financial Reporting Framework

- A4. Factors that are relevant to the auditor's determination of the acceptability of the financial reporting framework to be applied in the preparation of the financial report include:
- The nature of the entity (for example, whether it is a business enterprise, a public sector entity or a not for profit organisation);
  - The purpose of the financial report (for example, whether they are prepared to meet the common financial information needs of a wide range of users or the financial information needs of specific users);
  - The nature of the financial statements (for example, whether the financial statements are a complete set of financial statements or a single financial statement); and
  - Whether law or regulation prescribes the applicable financial reporting framework.
- A5. Many users of financial reports are not in a position to demand financial reports tailored to meet their specific information needs. While all the information needs of specific users cannot be met, there are financial information needs that are common to a wide range of users. Financial reports prepared in accordance with a financial reporting framework designed to meet the common financial information needs of a wide range of users are referred to as general purpose financial reports.
- A6. In some cases, the financial report will be prepared in accordance with a financial reporting framework designed to meet the financial information needs of specific users. Such financial reports are referred to as special purpose financial reports. The financial information needs of the intended users will determine the applicable financial reporting framework in these circumstances. ASA 800 (Revised and Redrafted) discusses the acceptability of financial reporting frameworks designed to meet the financial information needs of specific users.<sup>10</sup>
- A7. Deficiencies in the applicable financial reporting framework that indicate that the framework is not acceptable may be encountered

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<sup>10</sup> See ASA 800 (Revised and Redrafted) *Special Considerations—Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks*, paragraph 8.

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after the audit engagement has been accepted. When use of that framework is prescribed by law or regulation, the requirements of paragraphs 19-20 apply. When use of that framework is not prescribed by law or regulation, management may decide to adopt another framework that is acceptable. When management does so, as required by paragraph 16, new terms of the audit engagement are agreed to reflect the change in the framework as the previously agreed terms will no longer be accurate.

#### General purpose frameworks

A8. At present, there is no objective and authoritative basis that has been generally recognised globally for judging the acceptability of general purpose frameworks. In the absence of such a basis, financial reporting standards established by organisations that are authorised or recognised to promulgate standards to be used by certain types of entities are presumed to be acceptable for general purpose financial reports prepared by such entities, provided the organisations follow an established and transparent process involving deliberation and consideration of the views of a wide range of stakeholders. Examples of such financial reporting standards include:

- International Financial Reporting Standards (IFRSs) promulgated by the International Accounting Standards Board;
- International Public Sector Accounting Standards (IPSASs) promulgated by the International Public Sector Accounting Standards Board; and
- Accounting principles promulgated by an authorised or recognised standards setting organisation in a particular jurisdiction,\* provided the organisation follows an established and transparent process involving deliberation and consideration of the views of a wide range of stakeholders.

These financial reporting standards are often identified as the applicable financial reporting framework in law or regulation governing the preparation of general purpose financial reports.

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\* The Australian Accounting Standards Board (AASB) sets accounting standards in Australia.

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Financial reporting frameworks prescribed by law or regulation

- A9. In accordance with paragraph 6(a), the auditor is required to determine whether the financial reporting framework, to be applied in the preparation of the financial report, is acceptable. In some jurisdictions, law or regulation may prescribe the financial reporting framework to be used in the preparation of a general purpose financial report for certain types of entities. In the absence of indications to the contrary, such a financial reporting framework is presumed to be acceptable for a general purpose financial report prepared by such entities. In the event that the framework is not considered to be acceptable, paragraphs 19-20 apply.

Jurisdictions that do not have standards setting organisations or prescribed financial reporting frameworks

- A10. When an entity is registered or operating in a jurisdiction that does not have an authorised or recognised standards setting organisation, or where use of the financial reporting framework is not prescribed by law or regulation, management identifies a financial reporting framework to be applied in the preparation of the financial report. Appendix 2 contains guidance on determining the acceptability of financial reporting frameworks in such circumstances.

*Agreement of the Responsibilities of Management* (Ref: Para. 6(b))

- A11. An audit in accordance with Australian Auditing Standards is conducted on the premise that management has acknowledged and understands that it has the responsibilities set out in paragraph 6(b).<sup>11</sup> In certain jurisdictions, such responsibilities may be specified in law or regulation. In others, there may be little or no legal or regulatory definition of such responsibilities. Australian Auditing Standards do not override law or regulation in such matters. However, the concept of an independent audit requires that the auditor's role does not involve taking responsibility for the preparation of the financial report or for the entity's related internal control, and that the auditor has a reasonable expectation of obtaining the information necessary for the audit in so far as management is able to provide or procure it. Accordingly, the premise is fundamental to the conduct of an independent audit. To avoid misunderstanding, agreement is reached with management that it acknowledges and understands that it has such responsibilities as part of agreeing and recording the terms of the audit engagement in paragraphs 9-12.

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<sup>11</sup> See ASA 200 (Revised and Redrafted), paragraph A2.

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- A12. The way in which the responsibilities for financial reporting are divided between management and those charged with governance will vary according to the resources and structure of the entity and any relevant law or regulation, and the respective roles of management and those charged with governance within the entity. In most cases, management is responsible for execution while those charged with governance have oversight of management. In some cases, those charged with governance will have, or will assume, responsibility for approving the financial report or monitoring the entity's internal control related to financial reporting. In larger or publicly-listed entities, a subgroup of those charged with governance, such as an audit committee, may be charged with certain oversight responsibilities.
- A13. ASA 580 (Revised and Redrafted) requires the auditor to request management to provide written representations that it has fulfilled certain of its responsibilities.<sup>12</sup> It may therefore be appropriate to make management aware that receipt of such written representations will be expected, together with written representations required by other Australian Auditing Standards and, where necessary, written representations to support other audit evidence relevant to the financial report or one or more specific assertions in the financial report.
- A14. Where management will not acknowledge its responsibilities, or agree to provide the written representations, the auditor will be unable to obtain sufficient appropriate audit evidence.<sup>13</sup> In such circumstances, it would not be appropriate for the auditor to accept the audit engagement, unless law or regulation requires the auditor to do so. In cases where the auditor is required to accept the audit engagement, the auditor may need to explain to management the importance of these matters, and the implications for the auditor's report.

Preparation of the Financial Report (Ref: Para. 6(b)(i))

- A15. Most financial reporting frameworks include requirements relating to the presentation of the financial report; for such frameworks, *preparation* of the financial report in accordance with the financial reporting framework includes *presentation*. In the case of a fair presentation framework the importance of the reporting objective of fair presentation is such that the premise agreed with management includes specific reference to fair presentation, or to the

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<sup>12</sup> See ASA 580 (Revised and Redrafted) *Written Representations*, paragraphs 10-11.

<sup>13</sup> See ASA 580 (Revised and Redrafted), paragraph A26.

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responsibility to ensure that the financial report will “give a true and fair view” in accordance with the financial reporting framework.

Internal Control (Ref: Para. 6(b)(ii))

- A16. Management maintains such internal control as it determines is necessary to enable the preparation of the financial report that are free from material misstatement, whether due to fraud or error. Internal control, no matter how effective, can provide an entity with only reasonable assurance about achieving the entity’s financial reporting objectives due to the inherent limitations of internal control.<sup>14</sup>
- A17. An independent audit conducted in accordance with the Australian Auditing Standards does not act as a substitute for the maintenance of internal control necessary for the preparation of the financial report by management. Accordingly, the auditor is required to obtain the agreement of management that it acknowledges and understands its responsibility for internal control. However, the agreement required by paragraph 6(b)(ii) does not imply that the auditor will find that internal control maintained by management has achieved its purpose or will be free of deficiencies.
- A18. It is for management to determine what internal control is necessary to enable the preparation of the financial report. The term “internal control” encompasses a wide range of activities within components that may be described as the control environment; the entity’s risk assessment process; the information system, including the related business processes relevant to financial reporting, and communication; control activities; and monitoring of controls. This division, however, does not necessarily reflect how a particular entity may design, implement and maintain its internal control, or how it may classify any particular component.<sup>15</sup> An entity’s internal control (in particular, its accounting books and records, or accounting systems) will reflect the needs of management, the complexity of the business, the nature of the risks to which the entity is subject, and relevant laws or regulation.
- A19. In some jurisdictions, law or regulation may refer to the responsibility of management for the adequacy of accounting books and records, or accounting systems. In some cases, general practice may assume a distinction between accounting books and records or

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<sup>14</sup> See ASA 315 (~~Revised and Redrafted~~) *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph A46.

<sup>15</sup> See ASA 315 (~~Revised and Redrafted~~), paragraph A51 and Appendix 1.

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accounting systems on the one hand, and internal control or controls on the other. As accounting books and records, or accounting systems, are an integral part of internal control as referred to in paragraph A18, no specific reference is made to them in paragraph 6(b)(ii) for the description of the responsibility of management. To avoid misunderstanding, it may be appropriate for the auditor to explain to management the scope of this responsibility.

#### Considerations Relevant to Smaller Entities (Ref: Para. 6(b))

A20. One of the purposes of agreeing the terms of the audit engagement is to avoid misunderstanding about the respective responsibilities of management and the auditor. For example, when a third party has assisted with the preparation of the financial report, it may be useful to remind management that the preparation of the financial report in accordance with the applicable financial reporting framework remains its responsibility.

#### Management-Imposed Limitation of Scope

Aus A20.1 Section 312 of the *Corporations Act 2001 (Act)* requires an officer of the entity to allow the auditor access to the books of the entity and give any information, explanation or assistance required under section 310 of the Act. A management-imposed restriction of scope may breach section 312 and trigger the need for a section 311 notice to be provided by the auditor to the Australian Securities and Investments Commission (ASIC).

AUASB

## Agreement on Audit Engagement Terms

### *Agreeing the Terms of the Audit Engagement* (Ref: Para. 9)

A21. The roles of management and those charged with governance in agreeing the terms of the audit engagement for the entity depend on the governance structure of the entity and relevant law or regulation.

### *Audit Engagement Letter or Other Form of Written Agreement*<sup>16</sup> (Ref: Para. 10-11)

A22. It is in the interests of both the entity and the auditor that the auditor sends an audit engagement letter before the commencement of the audit to help avoid misunderstandings with respect to the audit. In

<sup>16</sup> In the paragraphs that follow, any reference to an audit engagement letter is to be taken as a reference to an audit engagement letter or other suitable form of written agreement.

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some countries, however, the objective and scope of an audit and the responsibilities of management and of the auditor may be sufficiently established by law, that is, they prescribe the matters described in paragraph 10. Although in these circumstances paragraph 11 permits the auditor to include in the engagement letter only reference to the fact that relevant law or regulation applies and that management acknowledges and understands its responsibilities as set out in paragraph 6(b), the auditor may nevertheless consider it appropriate to include the matters described in paragraph 10 in an engagement letter for the information of management.

#### Form and Content of the Audit Engagement Letter

A23. The form and content of the audit engagement letter may vary for each entity. Information included in the audit engagement letter on the auditor's responsibilities may be based on ASA 200 (Revised and Redrafted).<sup>17</sup> Paragraphs 6(b) and 12 of this Auditing Standard deal with the description of the responsibilities of management. In addition to including the matters required by paragraph 10, an audit engagement letter may make reference to, for example:

- Elaboration of the scope of the audit, including reference to applicable legislation, regulations, Australian Auditing Standards, and ethical and other pronouncements of professional bodies to which the auditor adheres.
- The form of any other communication of results of the audit engagement.
- The fact that because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with Australian Auditing Standards.
- Arrangements regarding the planning and performance of the audit, including the composition of the audit team.
- The expectation that management will provide written representations (see also paragraph A13).
- The agreement of management to make available to the auditor a draft financial report and any accompanying other

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<sup>17</sup> See ASA 200 (Revised and Redrafted), paragraphs 3-9.

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information in time to allow the auditor to complete the audit in accordance with the proposed timetable.

- The agreement of management to inform the auditor of facts that may affect the financial report, of which management may become aware during the period from the date of the auditor's report to the date the financial report is issued.
- The basis on which fees are computed and any billing arrangements.
- A request for management to acknowledge receipt of the audit engagement letter and to agree to the terms of the engagement outlined therein.

A24. When relevant, the following points could also be made in the audit engagement letter:

- Arrangements concerning the involvement of other auditors and experts in some aspects of the audit.
- Arrangements concerning the involvement of internal auditors and other staff of the entity.
- Arrangements to be made with the predecessor auditor, if any, in the case of an initial audit.
- Any restriction of the auditor's liability when such possibility exists.
- A reference to any further agreements between the auditor and the entity.
- Any obligations to provide audit working papers to other parties.

An example of an audit engagement letter is set out in Appendix 1.

**Audits of Components**

A25. When the auditor of a parent entity is also the auditor of a component,\* the factors that may influence the decision whether to

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\* See ASA 600 *Special Considerations – Audits of a Group Financial Report (Including the Work of Component Auditors)* (Revised and Redrafted).

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send a separate audit engagement letter to the component include the following:

- Who appoints the component auditor;
- Whether a separate auditor's report is to be issued on the component;
- Legal requirements in relation to audit appointments;
- Degree of ownership by parent; and
- Degree of independence of the component management from the parent entity.

**Responsibilities of Management Prescribed by Law or Regulation**  
(Ref: Para. 11-12)

A26. If, in the circumstances described in paragraphs A22 and A27, the auditor concludes that it is not necessary to record certain terms of the audit engagement in an audit engagement letter, the auditor is still required by paragraph 11 to seek the written agreement from management that it acknowledges and understands that it has the responsibilities set out in paragraph 6(b). However, in accordance with paragraph 12, such written agreement may use the wording of the law or regulation if such law or regulation establishes responsibilities for management that are equivalent in effect to those described in paragraph 6(b). The accounting profession, audit standards setter, or audit regulator in a jurisdiction may have provided guidance as to whether the description in law or regulation is equivalent.

**Considerations specific to public sector entities**

A27. Law or regulation governing the operations of public sector audits generally mandate the appointment of a public sector auditor and commonly set out the public sector auditor's responsibilities and powers, including the power to access an entity's records and other information. When law or regulation prescribes in sufficient detail the terms of the audit engagement, the public sector auditor may nonetheless consider that there are benefits in issuing a fuller audit engagement letter than permitted by paragraph 11.

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**Recurring Audits** (Ref: Para. 13)

A28. The auditor may decide not to send a new audit engagement letter or other written agreement each period. However, the following factors may make it appropriate to revise the terms of the audit engagement or to remind the entity of existing terms:

- Any indication that the entity misunderstands the objective and scope of the audit.
- Any revised or special terms of the audit engagement.
- A recent change of senior management.
- A significant change in ownership.
- A significant change in nature or size of the entity's business.
- A change in legal or regulatory requirements.
- A change in the financial reporting framework adopted in the preparation of the financial report.
- A change in other reporting requirements.

**Acceptance of a Change in the Terms of the Audit Engagement**

*Request to Change the Terms of the Audit Engagement* (Ref: Para. 14)

A29. A request from the entity for the auditor to change the terms of the audit engagement may result from a change in circumstances affecting the need for the service, a misunderstanding as to the nature of an audit as originally requested or a restriction on the scope of the audit engagement, whether imposed by management or caused by other circumstances. The auditor, as required by paragraph 14, considers the justification given for the request, particularly the implications of a restriction on the scope of the audit engagement.

A30. A change in circumstances that affects the entity's requirements or a misunderstanding concerning the nature of the service originally requested may be considered a reasonable basis for requesting a change in the audit engagement.

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A31. In contrast, a change may not be considered reasonable if it appears that the change relates to information that is incorrect, incomplete or otherwise unsatisfactory. An example might be where the auditor is unable to obtain sufficient appropriate audit evidence regarding receivables and the entity asks for the audit engagement to be changed to a review engagement to avoid a qualified opinion or a disclaimer of opinion.

**Request to Change to a Review or a Related Service (Ref: Para. 15)**

A32. Before agreeing to change an audit engagement to a review or a related service, an auditor who was engaged to perform an audit in accordance with Australian Auditing Standards may need to assess, in addition to the matters referred to in paragraphs A29-A31 above, any legal or contractual implications of the change.

A33. If the auditor concludes that there is reasonable justification to change the audit engagement to a review or a related service, the audit work performed to the date of change may be relevant to the changed engagement; however, the work required to be performed and the report to be issued would be those appropriate to the revised engagement. In order to avoid confusing the reader, the report on the related service would not include reference to:

- (a) The original audit engagement; or
- (b) Any procedures that may have been performed in the original audit engagement, except where the audit engagement is changed to an engagement to undertake agreed-upon procedures and thus reference to the procedures performed is a normal part of the report.

**Additional Considerations in Engagement Acceptance**

***Financial Reporting Standards Supplemented by Law or Regulation***

(Ref: Para. 18)

A34. In some jurisdictions, law or regulation may supplement the financial reporting standards established by an authorised or recognised standards setting organisation with additional requirements relating to the preparation of the financial report. In those jurisdictions, the applicable financial reporting framework for the purposes of applying the Australian Auditing Standards encompasses both the identified financial reporting framework and such additional requirements provided they do not conflict with the

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identified financial reporting framework. This may, for example, be the case when law or regulation prescribes disclosures in addition to those required by the financial reporting standards or when they narrow the range of acceptable choices that can be made within the financial reporting standards.<sup>18</sup>

#### *Financial Reporting Framework Prescribed by Law or Regulation—Other Matters Affecting Acceptance* (Ref: Para. 19)

- A35. Law or regulation may prescribe that the wording of the auditor's opinion use the phrases "present fairly, in all material respects" or "give a true and fair view" in a case where the auditor concludes that the applicable financial reporting framework prescribed by law or regulation would otherwise have been unacceptable. In this case, the terms of the prescribed wording of the auditor's report are significantly different from the requirements of Australian Auditing Standards (see paragraph 21).

#### *Auditor's Report Prescribed by Law or Regulation* (Ref: Para. 21)

- A36. Australian Auditing Standards require that the auditor shall not represent compliance with Australian Auditing Standards unless the auditor has complied with all of the Australian Auditing Standards relevant to the audit.<sup>19</sup> When law or regulation prescribes the layout or wording of the auditor's report in a form or in terms that are significantly different from the requirements of Australian Auditing Standards and the auditor concludes that additional explanation in the auditor's report cannot mitigate possible misunderstanding, the auditor may consider including a statement in the auditor's report that the audit is not conducted in accordance with Australian Auditing Standards-. The auditor is, however, encouraged to apply Australian Auditing Standards-, including the Australian Auditing Standards that address the auditor's report, to the extent practicable, notwithstanding that the auditor is not permitted to refer to the audit being conducted in accordance with Australian Auditing Standards.

#### Considerations Specific to Public Sector Entities

- A37. In the public sector, specific requirements may exist within the legislation governing the audit mandate; for example, the auditor

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<sup>18</sup> See ASA 700 (~~Revised and Redrafted~~), paragraph 15, includes a requirement regarding the evaluation of whether the financial report adequately refers to or describes the applicable financial reporting framework.

<sup>19</sup> See ASA 200 (~~Revised and Redrafted~~), paragraph 20.

may be required to report directly to a minister, the legislature or the public if the entity attempts to limit the scope of the audit.

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**Conformity with International Standards on Auditing**

This Auditing Standard conforms with International Standard on Auditing ISA 210 *Agreeing the Terms of Audit Engagements* ~~(Redrafted)~~, issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been added to this Auditing Standard (and do not appear in the text of the equivalent ISA) are identified with the prefix “Aus”.

Compliance with this Auditing Standard enables compliance with ISA 210.

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## Appendix 1

(Ref: Paras. A23-A24)

### Example of an Audit Engagement Letter

The following is an example of an audit engagement letter for an audit of a general purpose financial report prepared in accordance with Australian Accounting Standards and the *Corporations Act 2001*. This letter is not authoritative but is intended only to be a guide that may be used in conjunction with the considerations outlined in this Auditing Standard. It will need to be varied according to individual requirements and circumstances. It is drafted to refer to the audit of a financial report for a single reporting period and would require adaptation if intended or expected to apply to recurring audits (see paragraph 13 of this Auditing Standard). It may be appropriate to seek legal advice that any proposed letter is suitable.

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To the appropriate representative of management or those charged with governance of ABC Company:<sup>20</sup>

*[The objective and scope of the audit]*

You<sup>21</sup> have requested that we audit the financial report of ABC Company Ltd., which comprise the statement of financial position as at 30 June 20X1 and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration. We are pleased to confirm our acceptance and our understanding of this audit engagement by means of this letter. Our audit will be conducted with the objective of our expressing an opinion on the financial report.

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<sup>20</sup> The addressees and references in the letter would be those that are appropriate in the circumstances of the engagement, including the relevant jurisdiction. It is important to refer to the appropriate persons – see paragraph A21. For an audit under the *Corporations Act 2001*, the appropriate persons are the Directors.

<sup>21</sup> Throughout this letter, references to “you,” “we,” “us,” “management,” “those charged with governance” and “auditor” would be used or amended as appropriate in the circumstances.

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*[The responsibilities of the auditor]*

We will conduct our audit in accordance with Australian Auditing Standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial report is free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial report.

Because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with Australian Auditing Standards.

In making our risk assessments, we consider internal control relevant to the entity's preparation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. However, we will communicate to you in writing concerning any significant deficiencies in internal control relevant to the audit of the financial report that we have identified during the audit.

*[The responsibilities of management and identification of the applicable financial reporting framework (for purposes of this example, it is assumed that the auditor has not determined that the law or regulation prescribes those responsibilities in appropriate terms; the descriptions in paragraph 6(b) of this Auditing Standard are therefore used).]*

Our audit will be conducted on the basis that [management and, where appropriate, those charged with governance]<sup>22</sup> acknowledge and understand that they have responsibility:

- (a) For the preparation of the financial report that gives a true and fair view in accordance with the *Corporations Act 2001* and Australian Accounting Standards;<sup>23</sup>

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<sup>22</sup> Use terminology as appropriate in the circumstances. For an audit under the *Corporations Act 2001*, the appropriate terminology is the Directors.

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- (b) For such internal control as [management] determines is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error; and
- (c) To provide us with:
  - (i) Access to all information of which the directors and management ~~is~~ are aware that is relevant to the preparation of the financial report such as records, documentation and other matters;
  - (ii) Additional information that we may request from the directors and management for the purpose of the audit; and
  - (iii) Unrestricted access to persons within the entity from whom we determine it necessary to obtain audit evidence.

As part of our audit process, we will request from [management and, where appropriate, those charged with governance], written confirmation concerning representations made to us in connection with the audit.

We look forward to full cooperation from your staff during our audit.

[Other relevant information]

[Insert other information, such as fee arrangements, billings and other specific terms, as appropriate.]

[Reporting]

[Insert appropriate reference to the expected form and content of the auditor's report.]

The form and content of our report may need to be amended in the light of our audit findings.

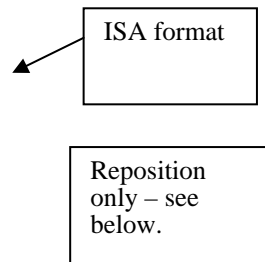
**Other Matters under the Corporations Act 2001**

*Independence*

We confirm that, to the best of our knowledge and belief, we currently meet the independence requirements of the *Corporations Act 2001* in relation to

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<sup>23</sup> Or, for financial reports not prepared under the *Corporations Act 2001*, “For the preparation and fair presentation of the financial report in accordance with Australian Accounting Standards.”



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the audit of the financial report. In conducting our audit of the financial report, should we become aware that we have contravened the independence requirements of the *Corporations Act 2001*, we shall notify you on a timely basis. As part of our audit process, we shall also provide you with a written independence declaration as required by the *Corporations Act 2001*.

The *Corporations Act 2001* includes specific restrictions on the employment relationships that can exist between the audited entity and its auditors. To assist us in meeting the independence requirements of the *Corporations Act 2001*, and to the extent permitted by law and regulation, we request you discuss with us:

- the provision of services offered to you by [insert firm name] prior to engaging or accepting the service; and
- the prospective employment opportunities of any current or former partner or professional employee of [insert firm name] prior to the commencement of formal employment discussions with the current or former partner or professional employee.

#### *Annual General Meetings*

The *Corporations Act 2001* provides that shareholders can submit written questions to the auditor before an Annual General Meeting provided that they relate to the auditor's report or the conduct of the audit. To assist us in meeting this requirement in the *Corporations Act 2001* relating to Annual General Meetings, we request you provide to us written questions submitted to you by shareholders as soon as practicable after the question(s) is received and no later than five business days before the Annual General Meeting, regardless of whether you believe them to be irrelevant.

#### **Presentation of Audited Financial Report on the Internet**

It is our understanding that the entity intends to publish a hard copy of the audited financial report and auditor's report for members, and to electronically present the audited financial report and auditor's report on its internet web site. When information is presented electronically on a web site, the security and controls over information on the web site should be addressed by the entity to maintain the integrity of the data presented. The examination of the controls over the electronic presentation of audited financial information on the entity's web site is beyond the scope of the audit of the financial report. Responsibility for the electronic presentation of the financial report on the entity's web site is that of the governing body of the entity.

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*~~{Other relevant information}~~*

*~~{Insert other information, such as fee arrangements, billings and other specific terms, as appropriate.}~~*

~~We look forward to full cooperation from your staff during our audit.~~

*~~{Reporting}~~*

*~~{Insert appropriate reference to the expected form and content of the auditor's report.}~~*

~~The form and content of our report may need to be amended in the light of our audit findings.~~

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our audit of the financial report including our respective responsibilities.

XYZ & Co.

Acknowledged and agreed on behalf of ABC Company Ltd. by

(signed)

.....

Name and Title

Date

Reposition only – see above.
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## Appendix 2

(Ref: Para. A10)

### Determining the Acceptability of General Purpose Frameworks

#### Jurisdictions that Do Not Have Authorised or Recognised Standards Setting Organisations or Financial Reporting Frameworks Prescribed by Law or Regulation

1. As explained in paragraph A10 of this Auditing Standard, when an entity is registered or operating in a jurisdiction that does not have an authorised or recognised standards setting organisation, or where use of the financial reporting framework is not prescribed by law or regulation, management identifies an applicable financial reporting framework. Practice in such jurisdictions is often to use the financial reporting standards established by one of the organisations described in paragraph A8 of this Auditing Standard.
2. Alternatively, there may be established accounting conventions in a particular jurisdiction that are generally recognised as the financial reporting framework for a general purpose financial report prepared by certain specified entities operating in that jurisdiction. When such a financial reporting framework is adopted, the auditor is required by paragraph 6(a) of this Auditing Standard to determine whether the accounting conventions collectively can be considered to constitute an acceptable financial reporting framework for a general purpose financial report. When the accounting conventions are widely used in a particular jurisdiction, the accounting profession in that jurisdiction may have considered the acceptability of the financial reporting framework on behalf of the auditors. Alternatively, the auditor may make this determination by considering whether the accounting conventions exhibit attributes normally exhibited by acceptable financial reporting frameworks (see paragraph 3 below), or by comparing the accounting conventions to the requirements of an existing financial reporting framework considered to be acceptable (see paragraph 4 below).
3. Acceptable financial reporting frameworks normally exhibit the following attributes that result in information provided in financial reports that is useful to the intended users:
  - (a) Relevance, in that the information provided in the financial report is relevant to the nature of the entity and the purpose

of the financial report. For example, in the case of a business enterprise that prepares a general purpose financial report, relevance is assessed in terms of the information necessary to meet the common financial information needs of a wide range of users in making economic decisions. These needs are ordinarily met by presenting the financial position, financial performance and cash flows of the business enterprise.

- (b) Completeness, in that transactions and events, account balances and disclosures that could affect conclusions based on the financial report are not omitted.
- (c) Reliability, in that the information provided in the financial report:
  - (i) Where applicable, reflects the economic substance of events and transactions and not merely their legal form; and
  - (ii) Results in reasonably consistent evaluation, measurement, presentation and disclosure, when used in similar circumstances.
- (d) Neutrality, in that it contributes to information in the financial report that is free from bias.
- (e) Understandability, in that the information in the financial report is clear and comprehensive and not subject to significantly different interpretation.

4. The auditor may decide to compare the accounting conventions to the requirements of an existing financial reporting framework considered to be acceptable. For example, the auditor may compare the accounting conventions to IFRSs. For an audit of a small entity, the auditor may decide to compare the accounting conventions to a financial reporting framework specifically developed for such entities by an authorised or recognised standards setting organisation. When the auditor makes such a comparison and differences are identified, the decision as to whether the accounting conventions adopted in the preparation ~~and presentation~~ of the financial report constitute an acceptable financial reporting framework includes considering the reasons for the differences and whether application of the accounting conventions, or the

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description of the financial reporting framework in the financial report, could result in a financial report that are misleading.

5. A conglomeration of accounting conventions devised to suit individual preferences is not an acceptable financial reporting framework for a general purpose financial report. Similarly, a compliance framework will not be an acceptable financial reporting framework, unless it is generally accepted in the particular jurisdictions by preparers and users.

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