

GS 007

(September 2011)

Guidance Statement GS 007
*Audit Implications of the use
of Service Organisations for
Investment Management
Services*

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

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Australian Government

Auditing and Assurance Standards Board

Guidance Statement GS 007 *Audit Implications of the use of Service Organisations for Investment Management Services*

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Draft

AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) formulates Guidance Statement GS 007 *Audit Implications of the use of Service Organisations for Investment Management Services*, pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001*, for the purposes of providing guidance on auditing and assurance matters.

This Guidance Statement provides guidance to assist the auditor to fulfil the objectives of the audit or assurance engagement. It includes explanatory material on specific matters for the purposes of understanding and complying with AUASB Standards. The auditor exercises professional judgement when using this Guidance Statement.

The Guidance Statement does not prescribe or create new requirements.

Dated: <TypeHere>

M H Kelsall
Chairman - AUASB

GUIDANCE STATEMENT GS 007

Audit Implications of the use of Service Organisations for Investment Management Services

Application

1. This Guidance Statement has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to:
 - (a) auditors (user auditors) of a financial report of an entity (user entity) which uses a service organisation to provide investment management services; and
 - (b) auditors (service auditors) of those service organisations, who provide reports on controls or financial information which may be used as audit evidence in the audit of the user entity's financial report.

Issuance Date

2. This Guidance statement is issued on xx xxxx 2011 by the AUASB and replaces 007 *Audit Implications of the use of Service Organisations for Investment Management Services*, issued in March 2008. It is operative for reporting periods commencing on or after 1 January 2012.

Introduction

3. This Guidance Statement applies to:
 - (a) the user auditor engaged to audit the financial report of an entity (user entity) that uses a third party service organisation to provide investment management services, where:

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- (i) the services provided are part of the user entity's information system, including related business processes, relevant to financial reporting;¹
- (ii) audit evidence required by the user auditor, regarding internal controls and/or assertions, is located at the service organisation; and
- (iii) reports on controls at the service organisation and/or a service auditor's report on specified assertions or a financial statement of the user entity's balances or transactions relating to the services provided by the service organisation are available.

Part A of this Guidance Statement (paragraphs 15-59) provides guidance to the user auditor on the application of Auditing Standard ASA 402, when using a service auditor's report on controls and/or Australian Auditing Standards, when using a service auditor's report on financial information, in the above circumstances.

- (b) The service auditor engaged to report on controls and/or financial information relating to components of user entities for which investment management services are provided by the service organisation.

Part B of this Guidance Statement (paragraphs 60-144) provides guidance to the service auditor on the application of Standard on Assurance Engagements ASAE 3402² when reporting on controls and Auditing Standard ASA 805³ when reporting on financial information.

¹ See ASA 402 *Audit Considerations Relating to an Entity Using a Service Organisation*, paragraph 3 which specifies when the service organisation's services are part of the user entity's information system, including related business processes, relevant to financial reporting.

² See ASAE 3402 *Assurance Reports on Controls at a Service Organisation*.

³ See ASA 805 *Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement*.

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4. User auditors are required to meet the requirements of ASA 402 when auditing a financial report or historical financial information of a user entity which uses the services of a service organisation. Service auditors are required to meet the requirements of ASAE 3402, when preparing an assurance report on controls at the service organisation, and the requirements of the Australian Auditing Standards, when reporting on financial information of the user entity held at the service organisation, for use by user entities and their auditors. This guidance statement provides additional guidance to user and service auditors when applying those standards, if investment management services are provided, and so is to be read in conjunction with those standards.

Types of Reports

5. This Guidance Statement provides guidance for the preparation and use as audit evidence of the following reports:
- (a) Reports on the description and design of controls at a service organisation (Type 1 report)⁴ or description, design and operating effectiveness of controls at a service organisation (Type 2 report),⁵ relating to the service organisation's system over the investment management services provided to user entities, prepared in accordance with ASAE 3402.
 - (b) Service auditor's reports on financial information, prepared in accordance with ASA 805,⁶ comprising either:
 - (i) a service auditor's report on specified assertions regarding balances or transactions of the user entity reported in a financial statement by the service organisation, which provides investment management services, ("Service Auditor's Report on Specified Assertions"); or

⁴ See ASAE 3420, paragraph 9(j).

⁵ See ASAE 3420, paragraph 9(k).

⁶ ASA 800 is also applicable if the financial information is a financial report or complete set of financial statements prepared in accordance with a special purpose framework.

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- (ii) a service auditor's report on a financial statement of the user entity's balances or transactions ("Statement") reported by the service organisation which provides investment management services ("Service Auditor's Report on a Statement").
- 6. Type 1 and 2 reports on controls comprise:⁷
 - (a) A service organisation's description of its investment management services system, including identification of: the services covered; the date or period to which the description relates; control objectives, including the control objectives listed in Appendix 2 Example 2 of this Guidance Statement for the relevant investment management services provided; and related controls.⁸
 - (b) A written assertion by the service organisation that, in all material respects, and based on suitable criteria: the description fairly presents the service organisation's system as designed and implemented and that the controls related to the control objectives stated in the service organisation's description of its system were suitably designed as at the specified date, for a Type 1 Report, or throughout the period, for a Type 2 Report. In addition, for a Type 2 Report, an assertion that the controls operated effectively throughout the specified period.
 - (c) A service auditor's assurance report that conveys reasonable assurance about the service organisation's assertions, including for Type 2 Reports, a description of the tests of controls and the results thereof.
- 7. The use of a Type 1 report by a user auditor is limited to understanding the entity in accordance with Auditing Standard 315,⁹ whereas a Type 2 report may also be used by a user auditor in

⁷ See ASAE 3402, paragraph 9(j) & 9(k).

⁸ See ASAE 3402, paragraph 9(n).

⁹ See ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.

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responding to assessed risks in accordance with Auditing Standard ASA 330.¹⁰

8. Other reports may be required by the user entity as set out in the contract and/or service level agreement for purposes such as monitoring the performance of the service organisation, however the reports covered by this Guidance Statement are limited to those that may be used by user auditors as audit evidence for the audit of the user entity's financial report.
9. The following table, entitled *Table 1: Service Auditor's Reports*, outlines the context in which each of these reports is prepared and used as audit evidence. Table 1 lists the reports included in this Guidance Statement, the subject matter covered by each report, the circumstances for which each report may be useful to user auditors, standards relevant to the preparation and use of each report and references to appendices containing examples of each report and related engagement letters.

¹⁰ See ASA 330 *The Auditor's Responses to Assessed Risks*.

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Table 1: Service Auditor's Reports

Title of Report	Subject Matter Covered by Report	Circumstances for Which Report is Used by User Auditors	Relevant Standards	Appendix Reference for Examples
Reports on controls				
1. Type 1 Report	Description and design of controls at the service organisation.	Planning: Obtaining an understanding of the user entity and its environment, including controls over services provided by the service organisation, in order to assess the risk of material misstatement and design further audit procedures. This report cannot be relied on to reduce substantive procedures.	User Auditor: ASA 402 & ASA 315 ¹¹ Service Auditor: ASAE 3402	Engagement letter: Appendix 1 Example 1 Service Auditor's Type 1 Report: No example provided as this report is not likely to meet the needs of all user auditors.

¹¹ See ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.

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Title of Report	Subject Matter Covered by Report	Circumstances for Which Report is Used by User Auditors	Relevant Standards	Appendix Reference for Examples
2. Type 2 Report	Description, design, & operating effectiveness of controls at the service organisation.	<p>Planning: Obtaining an understanding of the user entity and its environment: as for Type 1 Reports.</p> <p>Responding to the assessed risks of material misstatement when evidence is required of the operating effectiveness of controls, over the services provided, at the service organisation</p>	<p>User Auditor: ASA 402 & ASA 330</p> <p>Service Auditor: ASAE 3402</p>	<p>Engagement letter: Appendix 1 Example 1</p> <p>Service Organisation's Description of its System and Assertion: Appendix 2;</p> <p>Minimum Control Objectives: Appendix 3;</p> <p>Service Auditor's Type 2 Report: Appendix 4 and Appendix 5.</p>

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Title of Report	Subject Matter Covered by Report	Circumstances for Which Report is Used by User Auditors	Relevant Standards	Appendix Reference for Examples
Service Auditor's reports on financial information				
3. Service Auditor's Report on Specified Assertions	Specified assertions regarding balances or transactions of the user entity reported in a Statement.	Require evidence from procedures conducted at the service organisation regarding certain assertions with respect to balances or transactions of the user entity, reported in a Statement.	Service Auditor: ASA 805	Engagement letter: Appendix 1 Example 2 Service Auditor's Report: Appendix 6 Example 1
4. Service Auditor's Report on a Statement	Balances or transactions of the user entity reported in a Statement.	Require evidence from procedures conducted at the service organisation regarding the balances or transactions of the user entity, reported in a Statement.	Service Auditor: ASA 805	Engagement letter: Appendix 1 Example 3 Service Auditor's Report: Appendix 6 Example 2

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10. The guidance in this Guidance Statement is based on engagements to provide an opinion based on reasonable assurance, with respect to controls or financial information. It does not apply to an engagement to provide a review conclusion on controls based on limited assurance, however, it may be adapted, as necessary in the circumstances, to an engagement to provide limited assurance on specified assertions or a Statement. A review conclusion from the service auditor may be appropriate where the user auditor is engaged to perform a review of the user entity's financial report. The service auditor exercises professional judgement in applying this Guidance Statement to a review and, when reporting on specified assertions or a Statement, complies with the requirements of relevant standards on review engagements.
11. The user auditor may request the user entity to obtain a service auditor's report on agreed-upon procedures. Agreed-upon procedures engagements may be appropriate in certain circumstances to provide evidence that the user auditor requires, for example when:
- A Type 2 report is provided, however the user auditor requires more evidence with respect to controls over a specified area, such as unit pricing.
 - Provision of service auditor reports is not agreed in the service level agreement or contract, but the user auditor nevertheless requires selected controls to be tested at the service organisation.
 - A Service Auditor's Report on Specified Assertions is provided as described in this Guidance Statement, however further audit procedures are required by the user auditor in obtaining sufficient appropriate audit evidence with respect to particular assertions. For example, with respect to the assertion of valuation, agreement of valuation input variables to source data may be required by the user auditor.

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Such engagements are conducted under Standards on Related Services¹² and no further guidance on agreed-upon procedures engagements is provided in this Guidance Statement.

Services Relevant to this Guidance Statement

12. This Guidance Statement has been developed specifically for circumstances where service organisations provide investment management services to user entities, where those services and the controls over them, are part of the user entity's information system, including business processes, relevant to financial reporting,¹³ and as a result are relevant to the audit of a user entity's financial report. The Investment Management Services addressed in this guidance statement are:

- Custody.
- Asset Management.
- Property Management.
- Superannuation Member Administration.
- Investment Administration.
- Registry.

Each of these services are defined in Appendix 3.

13. Although this Guidance Statement has been written in the context of the service organisation providing any of the investment management services specified in paragraph 12 user and service auditors may use this Guidance Statement, as appropriate, where the service organisation provides other services which are part of the user entity's information system relevant to financial reporting.

¹² See ASRS 4400 *Agreed-upon Procedures Engagements to Report Factual Findings*.

¹³ The circumstances under which a service organisation's services are part of a user entity's information system, including business processes, relevant to financial reporting, are provided in ASA 402 paragraph 3.

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14. Operators of investor directed portfolio services (IDPS)¹⁴ and investor directed portfolio-like services are required by ASIC Class Order 02/294¹⁵ and Class Order 02/296¹⁶ to obtain an auditor's report providing an opinion on the internal controls and other relevant accounting procedures as they relate to the specific annual investor statements, and a review conclusion on the annual investor statements, quarterly reports in certain circumstances and information accessible to clients electronically. These class orders provide requirements for the form and content of the report in these circumstances. Reports provided under these class orders may provide sufficient appropriate audit evidence for a user auditor. If additional evidence is required by the user auditor, a service auditor's report on controls or on financial information may be requested. IDPS or IDPS-like services generally include custody and investment administration, consequently, if a Type 1 or 2 report is provided the user auditor can reasonably expect the operator (service organisation) and service auditor of an IDPS to report on the control objectives for the relevant services provided in this guidance statement.
15. Types of service organisations which provide some or all of these investment management services include:
- Custodians.
 - Third Party Administrators.
 - Investment Managers.
 - Registrars.

¹⁴ "IDPS" means an investor directed portfolio service, consisting of a number of functions including a custody, settlement and reporting system and service. The clients of the service have the sole discretion to decide what assets will be acquired or disposed of. The service is provided in such a way that clients are led to expect, and are likely to receive, benefits in the form of access to investments that the client could not otherwise access directly or cost reductions by using assets contributed by the client or derived directly or indirectly from assets contributed by the client with assets contributed by other clients or derived directly or indirectly from assets contributed by other clients.

¹⁵ See ASIC Class Order 02/294 *Investor Directed Portfolio Services*.

¹⁶ See ASIC Class Order 02/296 *Investor Directed Portfolio-like Services provided through a registered managed investment Scheme*.

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- Trust Departments of Financial Institutions.
 - Prime Brokers.
16. The responsible parties which typically engage the services of these service organisations on behalf of user entities, include but are not limited to:
- Trustees for Superannuation Funds.
 - Responsible Entities for Registered Managed Investment Schemes.
 - Trustees for Unregistered Unit Trusts.
 - Boards of Insurance Companies.
17. The responsibilities of the responsible party of a user entity are set out in the relevant laws and regulations governing their role and the particular services they oversee.

A: GUIDANCE FOR THE USER AUDITOR

18. The use of a service organisation for the provision of investment management services by a user entity does not alter the overall objective of the audit of the user entity's financial report, therefore it remains the responsibility of the user auditor to obtain sufficient appropriate audit evidence to support the auditor's opinion. The requirements of the Auditing Standards relating to obtaining sufficient appropriate evidence on which to form an opinion are the same as would apply if the records and supporting documentation were maintained by the user entity.

Using a Type 1 or Type 2 Report on Controls

19. ASA 402 provides requirements for the user auditor in obtaining an understanding of the user entity and its environment when the user entity uses the services of a service organisation¹⁷ and states that a Type 1 or 2 report may be used to obtain that understanding, if the user auditor is unable to obtain a sufficient understanding from the user entity.¹⁸ The user auditor is required to determine whether the Type 1 or 2 report provides sufficient and appropriate audit evidence to support the user auditor's understanding of the design and implementation of controls at the service organisation.¹⁹
20. A Type 1 Report cannot be relied upon to reduce the level of substantive procedures conducted by the user auditor, as it does not provide any evidence of the operating effectiveness of those controls. Consequently, the usefulness of a Type 1 Report to a user auditor is limited to planning the audit, assessing the risk of material misstatement and designing further audit procedures.
21. When the user auditor's risk assessment includes an expectation that controls at the service organisation are operating effectively, ASA 402 requires the user to obtain evidence about the operating effectiveness of those controls, which may be obtained from a Type 2 report.²⁰ Type 1 and 2 Reports are prepared for the purposes

¹⁷ See ASA 402, paragraphs 9-11.

¹⁸ See ASA 402, paragraph 12.

¹⁹ See ASA 402, paragraphs 13 & 14.

²⁰ See ASA 402, paragraph 16.

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of multiple user entities, not specifically for the purposes of any individual user auditor. The user auditor determines the sufficiency and appropriateness of the audit evidence provided by a Type 2 report in accordance with ASA 402.²¹

22. Whilst the user auditor makes their own assessment of the relevance of the service auditor's tests of controls to the assertions in the user entity's financial report, when investment management services are provided, the user auditor can reasonably expect:
- (a) each of the control objectives specified in this Guidance Statement²² for the relevant investment management service/s to be addressed in the service organisation's description of its system and assertion;
 - (b) the related controls identified to be reported on by the service auditor; and
 - (c) adequate justification to be provided by the service organisation for any control objectives for which no related controls are identified.
23. When the service organisation reports against the minimum control objectives provided in this guidance statement it assists the user auditor to:
- Compare directly the controls in place at different service organisations providing the same investment management services.
 - Collate the results of the controls tested where multiple service organisations are used to provide the same service.
 - Identify omissions in the user entity's description of the system or gaps in the system of control over the relevant investment management services.

²¹ See ASA 402, paragraph 17.

²² See Appendix 4, Minimum Control Objectives for each Investment Management Service.

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24. When assessing the sufficiency and appropriateness of the evidence provided by a Type 2 report, ASA 402²³ requires the user auditor to evaluate the adequacy of the time period covered and the time elapsed since performance of the tests of controls. Whilst the longer the time elapsed since the performance of the tests, the less evidence the test may provide, it is necessary for the Type 2 report to be available with sufficient time for the user auditor to use the evidence it contains prior to completion of the user entity's audit. It may be necessary for the user auditor to conduct further procedures in response to a modified opinion or deviations reported in the results of the tests performed. Consequently, a Type 2 report issued for a time period ending prior to the user entity's period end may be more useful for the user auditor, even if the user auditor needs to obtain additional evidence about the operation of controls in the intervening period.
25. When the service organisation has used a subservice organisation in providing investment management services to the user entity and those services are excluded from the Type 1 or 2 report, ASA 402 requires, if those services are relevant to the audit of the user entity, the user auditor to apply the requirements of ASA 402 with respect to the services of the subservice organisation.²⁴
26. If a Type 2 Report provides the user auditor with sufficient appropriate audit evidence as to the reliability of controls over the investment management services provided by the service organisation to the user entity then it will enable the user auditor to reduce the extent of substantive testing that might otherwise have been necessary with respect to the balances or transactions subject to those services.
27. Type 1 and 2 Reports are prepared for the purposes of multiple user entities, not specifically for the purposes of any individual user auditor. ASA 402 provides requirements as to how the user auditor

²³ See ASA 402, paragraph 17(c).

²⁴ See ASA 402, paragraph 18.

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uses a Type 2 report as audit evidence that controls at the service organisation are operating effectively.²⁵

28. A Type 2 report is not necessary, if the user auditor concludes that the risk of material misstatement will not be affected by the controls at the service organisation or that it is more appropriate to gather the evidence required by alternative procedures. These alternative procedures may include obtaining a Service Auditor's Report on financial information.

Using a Service Auditor's Report on Financial Information

29. In responding to the assessed risks of material misstatement, if sufficient appropriate audit evidence is not available from records held at the user entity, ASA 402 requires the user auditor to perform further audit procedures or use another auditor to perform those procedures at the service organisation.²⁶ Whilst the user auditor may be able to rely on a Type 2 Report as audit evidence of the operating effectiveness of controls to mitigate identified risks of material misstatement, a Type 2 Report alone cannot provide sufficient appropriate audit evidence with respect to material balances or classes of transactions of the user entity. ASA 330²⁷ requires the user auditor to design and perform substantive procedures for each material class of transactions, account balance and disclosure.
30. Service organisations which provide investment management services may provide the user entity with a single financial statement regarding financial information of the user entity ("Statement") periodically in accordance with either a general purpose framework²⁸ or special purpose framework²⁹. Examples of a Statement include: a portfolio valuation report, a financial report or a component of a financial report. The requirements of the applicable financial reporting framework determine the form and content of the Statement. An un-audited Statement is an unverified source of

²⁵ See ASA 402, paragraphs 17.

²⁶ See ASA 402, paragraph 15.

²⁷ See ASA 330 paragraph 18.

²⁸ See ASA 700, paragraph 7(b) for definition of general purpose framework.

²⁹ See ASA 800, paragraph 6(b) for definition of special purpose framework.

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evidence, which is a representation not independent from the user entity. If the financial report of the user entity has been prepared using un-audited financial information obtained from the service organisation, such information may not constitute sufficient appropriate audit evidence on which the user auditor could form an opinion.

31. The user auditor's procedures at the user entity with respect to the balances and transactions relating to the services provided by the service organisation are usually limited to:
- A review of the contract or service level agreement between the user entity and the service organisation so as to understand the rights and obligations of each party.
 - A review and evaluation of the monitoring controls exercised by the user entity over the service organisation.
 - A review of representations given by the service organisation concerning the user entity's balances or transactions.
 - Verification of the receipt of income from the service organisation (if not re-invested).
 - Analytical procedures on the financial information supplied by the service organisation.
 - A review of the most recent audited financial report of the service organisation.

These procedures alone, or even in combination with a Type 1 or 2 Report on controls over the relevant investment management services, may not generate sufficient appropriate audit evidence.

32. The user auditor exercises professional judgement to determine whether the results of procedures conducted at the user entity as described in paragraph 31, considered alone or in combination with a Type 1 or 2 Report, provide sufficient, appropriate evidence on which to form an audit opinion. If the user auditor requires further

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audit evidence, which the user auditor believes to be held at the service organisation, the user auditor either:

- (a) obtains a Service Auditor's Report on financial information; or
 - (b) gains access to the records and other information relating to the user entity in the possession of the service organisation.
33. Individual circumstances determine whether a Service Auditor's Report on financial information is the more effective or efficient method of obtaining the audit evidence required by the user auditor. If the user auditor is able to specify whether the service auditor prepares a Service Auditor's Report on specified assertion or on a Statement, the user auditor must exercise professional judgement to make this determination in the particular circumstances of the engagement.
34. A Service Auditor's Report on a Statement, as defined in paragraph 5(b)(ii), may be the most effective way to obtain sufficient appropriate audit evidence for all assertions regarding the user entity's balances or transactions contained in the Statement provided by the service organisation. This type of report may also be required by the user auditor if there is a potential or identified significant deficiency in the service organisation's controls, or there are material errors identified in the service organisation's reports.
35. The user auditor may be able to obtain sufficient appropriate audit evidence only for certain assertions relating to the user entity's balances or transactions contained in the Statement from information available from the user entity's records and from audit procedures performed thereon by the user auditor. For the remaining assertions, a Service Auditor's Report on Specified Assertions, as defined in paragraph 4(b)(i), could provide the audit evidence required. This may include any of the assertions identified in ASA 315,³⁰ which are:

³⁰ See ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph A111.

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- (a) for classes of transactions and events for the period under audit: occurrence, completeness, accuracy, cut-off and classification;
- (b) for account balances at the period end: existence, rights and obligations, completeness, valuation and allocation; and
- (c) for presentation and disclosure: occurrence and rights and obligations, completeness, classification and understandability and accuracy and valuation.

In many circumstances, the use of a Service Auditor's Report on Specified Assertions in conjunction with a Type 2 Report provide the user auditor with sufficient appropriate audit evidence concerning the balances or transactions reported in the Statement.

36. In evaluating the audit evidence provided by a Service Auditor's Report on financial information, the user auditor considers:
- (a) the professional competence of the service auditor in the context of the assignment conducted;
 - (b) the sufficiency and appropriateness of the evidence, whether on its own or in conjunction with a Type 1 or 2 Report, provided by the Service Auditor's report on financial information regarding the assertions on which evidence is required;
 - (c) the impact of any modification to the Service Auditor's Report on financial information on the sufficiency and appropriateness of the evidence provided by the report;
 - (d) the effect of any uncorrected misstatements reported by the service auditor in an attachment to their report, as described in paragraph 85; and
 - (e) the effect of any other matters, including significant deficiencies in internal control, significant findings from the audit or fraud, identified during the audit or reported by the service organisation to the user entity.

Materiality for Service Auditor's Reports on Financial Information

37. Paragraphs 79 to 81 of this Guidance Statement provide an appropriate basis for the service auditor to determine materiality for auditing specified assertions or a Statement. The user auditor, in determining performance materiality under Auditing Standard ASA 320³¹ for the classes of transactions, account balances or disclosures effected by the services of the service organisation, may determine that the performance materiality level which would be determined by the service auditor in applying this Guidance Statement is not suitable for the purposes of the audit of the user entity's financial report. In these circumstances, the user auditor may request that an alternative benchmark and/or percentage is used by the service auditor to determine performance materiality. The manner in which such a request is ordinarily communicated is discussed in paragraphs 39 and 40.
38. The user auditor makes the user auditor's own assessment of the materiality of any uncorrected misstatements communicated by the service auditor in the attachment, if any, to the Service Auditor's Report on financial information provided as described in paragraph 85, with respect to the audit of the user entity's financial report.

Communicating with the Service Auditor

39. Ordinarily, the user auditor does not communicate directly with the service auditor, communication is through the user entity and service organisation. The user auditor communicates requirements with respect to the service auditor's work as early as possible to the user entity. These requirements are then communicated by the user entity to the service organisation, either under the terms of a contract or service level agreement³² or by means of a specific request. In turn, these requirements are communicated by the service organisation to the service auditor and key requirements ordinarily are reflected in the service auditor's engagement letter with the service organisation.

³¹ See ASA 320 *Materiality in Planning and Performing an Audit*, paragraphs 11 & A12.

³² See ASA 402 paragraph A8.

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40. The user auditor's engagement letter may contain requirements for the user entity to obtain from the service organisation, where possible, Type 1 or 2 Reports or Service Auditor's Reports on financial information.

Communicating With Those Charged With Governance of the User Entity

41. The user auditor is required under the Auditing Standards to communicate any of the following matters identified to those charged with governance of the user entity on a timely basis:
- (a) significant deficiencies in internal control identified during the audit;³³
 - (b) significant findings from the audit;³⁴
 - (c) uncorrected misstatements and the effect they, individually or in aggregate, may have on the opinion in the auditor's report;³⁵ and
 - (d) fraud, identified or suspected involving management, employees who have significant roles in internal control or others where the fraud results in a material misstatement, as well as any other matters related to fraud that are relevant to their responsibilities.³⁶
42. In determining whether there are any matters which the user auditor needs to report to those charged with governance of the user entity, as outlined in paragraph 41, with respect to the investment management services provided by the service organisation, the user auditor's procedures may include:

³³ See ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*, paragraph 9.

³⁴ See ASA 260 *Communication with Those Charged with Governance*, paragraph 16.

³⁵ See ASA 450 *Evaluation of Misstatements Identified during the Audit*, paragraph 12.

³⁶ See ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*, paragraph 41 and 42.

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- A review of documentation and correspondence at the user entity regarding oversight and monitoring of the performance of the contract and/or service level agreement by the service organisation.
 - Enquiries of those charged with governance, management or others within the user entity regarding whether any of the matters listed in paragraph 41 have been reported by the service organisation to the user entity.
 - Identification of any exceptions reported by the service auditor in the Type 1 or 2 Report and evaluation of whether those exceptions represent significant deficiencies in the user entity's internal control.
 - Enquiries regarding the reasons for any modification to the Service Auditor's Type 1 or 2 Report or report on financial information.
 - Identification of any uncorrected misstatements reported by the service auditor, in an attachment to the Service Auditor's Report on financial information as described in paragraph 85 of this Guidance Statement.
43. If a Type 1 or 2 controls report is available, ASA 402³⁷ requires the user auditor to enquire of management of the user entity whether the service organisation has reported to the user entity, or the user entity is aware of, any fraud, non-compliance with laws and regulations or uncorrected misstatements affecting the financial report of the user entity. These matters of governance interest are required to be communicated to the user entity by the service organisation under ASAE 3402.³⁸ In addition, a service organisation may be required under the contract or service level agreement with the user entity to disclose matters including those listed in paragraph 41 that may affect the user entity. The user auditor evaluates the effect of any

³⁷ See ASA 402, paragraph 19.

³⁸ See ASAE 3402, paragraph 56.

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matters reported on the nature, timing and extent of further audit procedures.³⁹

44. Where the user auditor does not have sufficient information regarding the matters of governance interest to fulfil the user auditor's responsibility as outlined in paragraph 41 the user auditor may request further information to be provided. Whilst this information may be provided by the service auditor, the request is ordinarily made through the user entity.

Reporting by the User Auditor

45. If the user auditor concludes that the user entity's financial report contains material misstatements with respect to the services provided by the service organisation or that the user auditor is unable to obtain sufficient appropriate audit evidence regarding the services provided by the service organisation relevant to the audit to form an opinion, ASA 705 requires the user auditor to modify their opinion on the user entity's financial report.⁴⁰
46. In accordance with ASA 402⁴¹ and the Auditing Standards, when using a Type 1 or 2 report on controls or a service auditor's report on financial information, the user auditor does not refer to the work of a service auditor in the user auditor's report, unless required to do so by law or regulation or if it is relevant to understanding a modification to the user auditor's opinion.

³⁹ See ASA 402, paragraph A41.

⁴⁰ See ASA 705 *Modifications to the Opinion in the Independent Auditor's Report*, paragraph 6 and ASA 402, paragraph 20.

⁴¹ See ASA 402 paragraph 21 and 22.

B: GUIDANCE FOR THE SERVICE AUDITOR

Types of Engagements

47. Under a contract, offer document or service level agreement, the service organisation may agree to provide the user entity periodically with a Type 1 or 2 Report on controls, prepared in accordance with ASAE 3402, with respect to the services provided to the user entity and/or a Statement, with respect to the user entity's assets, liabilities or transactions recorded by the service organisation for the period, accompanied by a Service Auditor's Report on the Statement or specified assertions, issued in accordance with ASA 805.

Engagements to Report on Controls

Nature of Engagement

48. Service auditor's engagements to report on controls are assurance engagements, which are defined under the *Framework for Assurance Engagements* as engagements in which the auditor expresses a conclusion or opinion about the outcome of the evaluation of a subject matter against criteria. The criteria for an engagement to report on a service organisation controls, includes control objectives.⁴² [CG1] The control objectives collectively reflect the level of control over user entities' balances or transactions that the user entity could reasonably expect from the service organisation for the purpose of the user entity's financial reporting. The service organisation's controls are designed to meet those control objectives. Appendix 3 sets out the control objectives which the user entity can expect to be included in Type 1 or 2 Reports for each of the relevant investment management services. The service organisation may choose to include additional control objectives in the Type 1 or 2 Report. Additional control objectives may be included where those objectives are relevant to user entities' financial reporting or to meet compliance reporting requirements or the terms of the service level agreement, offer document or contract.

⁴² See ASAE 3402, paragraph 16.

Acceptance and Continuance of Engagements to Report on Controls

49. When agreeing to accept, or continue, an engagement to report on controls at a service organisation, ASAE 3402⁴³ requires the service auditor to assess whether the criteria will be suitable and available to user entities and their auditors. In doing so, the service auditor determines whether the criteria include the control objectives provided in this guidance statement for the relevant investment management services and, if any objectives are omitted, whether the service organisation has adequately disclosed and justified that omission.
50. An example of an engagement letter for engagements to report on controls is provided in Appendix 1 Example 1.

Ethical Requirements

51. ASAE 3402 requires the service the service auditor to comply with relevant ethical requirements including those pertaining to independence, relating to assurance engagements,⁴⁴ which does not necessitate the service auditor being independent from each user entity.
52. However, threats to independence may arise with respect to user entities where there are only one or few user entities for the services subject to audit. Threats to independence may also arise with respect to subservice organisations where the controls of the subservice organisation are included in the Service Organisation's description of its system, under the inclusive method.⁴⁵
53. Service auditors may also need to consider the manner in which their Type 1 or 2 Report is used and distributed by the service organisation. Examples of how this matter may be addressed in the engagement letter and in the Service Auditor's Type 2 Report are contained in Appendix 1 Example 1 and Appendix 4 respectively.

⁴³ See ASAE 3402, paragraphs 13 -18 for requirements in accepting and continuing an engagement to report on controls at a service organisation.

⁴⁴ See ASAE 3402, paragraph 11.

⁴⁵ See ASAE 3402, paragraph 9(g).

Responsibilities of the Service Organisation

54. It is for management, or, where appropriate, those charged with governance, of the service organisation to decide whether to prepare a report on controls and whether to have this report audited by a service auditor. In certain circumstances, the service organisation may, for example, consider it more appropriate to allow access for user entities and user auditors to the service organisation's records or provide a report on a specific aspect of its operations as this impacts an individual user entity. However, this Guidance Statement is only applicable to circumstances where management, or those charged with governance, of the service organisation prepares a description of its system, for example in a manner consistent with the reporting format illustrated in Appendix 2, and the service auditor is engaged to provide an opinion thereon, as illustrated in Appendix 4.
55. The service organisation typically prepares a description of its system to meet the needs of all user entities of a particular investment management service or services. The Service Auditor's Type 1 or 2 Report covers investment management services provided to user entities which are likely to form part of those user entities' information systems relevant to financial reporting. The value of a Type 1 Report to the audit of the user entity is limited, so it is appropriate for the service auditor to prepare a Type 1 Report only in the first year of reporting on controls, to provide a starting point for future reports, or if none of the user entities require a report on the operating effectiveness of controls. Circumstances in which the user auditor may require a report only on design and implementation of controls are set out in paragraph 20. Since these circumstances are limited, an example of this report is not provided in this Guidance Statement.
56. The frequency with which the service organisation provides a report on controls and the time period to be covered may be agreed in the contract and/or service level agreement between the user entity and the service organisation or may be set out in an offer document. It may be preferable for user auditors if the Type 1 or 2 report is for a period ending earlier than the user entity's reporting period end, in order to allow sufficient time for the user auditor to design and

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conduct further procedures in response to the results of the tests performed and any modifications in the service auditor's report.

57. An example of a Service Organisation's description of its system and assertion is shown in Appendix 2.

Assessing the Suitability of the Criteria

58. In assessing whether the service organisation has used suitable criteria in preparing the description of the system, evaluating whether controls are suitably designed and, in the case of Type 2 reports, in evaluating whether controls are operating effectively, in accordance with ASAE 3402,⁴⁶ the service auditor determines whether the minimum control objectives provided in this guidance statement⁴⁷ for the relevant investment management service or services are included in the description of the system.
59. It is the responsibility of the service organisation to ensure that the control objectives are sufficient to meet the expectations of user entities and that any omissions or amendments to the minimum control objectives are appropriate. A service organisation may therefore consider the need to add further objectives and supporting controls where appropriate. The service auditor evaluates the suitability of any additional control objectives specified by the service organisation, by determining if they meet the characteristics of relevance, completeness, reliability, neutrality and understandability.⁴⁸
60. If the service organisation omits or modifies a control objective from GS 007 or adds further control objectives, the service auditor can expect those omissions, modifications or additional objectives to be clearly identified in the service organisation's description of the system. If a control objective is omitted, the service organisation may list that objective and note briefly the reasons for its omission. If a control objective is modified to clarify the intended meaning, such as use of terms appropriate to the service organisation's

⁴⁶ See ASAE 3402, paragraphs 15-18 for further requirements in assessing the suitability of the criteria.

⁴⁷ See Appendix 3.

⁴⁸ See ASAE 3000, paragraph 35-36.

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circumstances, or the control objective is expanded, the relevant GS 007 control objective may be treated as included. However, if the meaning of the control objective is changed or the scope of the objective reduced by the modifications, then it is appropriate for the service organisation to report the relevant GS 007 objective as omitted and report the modified objective as an additional objective in the description of the system.

Obtaining an Understanding of the Service Organisation's System

61. ASAE 3402⁴⁹ requires the service auditor to obtain an understanding of the service organisation's system, including controls that are included in the scope of the engagement. In doing so, the service auditor identifies the boundaries of that system and ensures that the boundary of the investment management services included in the description of the system does not omit aspects of the services provided which are part of user entities' information system relevant to financial reporting. The description of each investment management services provided in this guidance statement is indicative and not definitive. The service organisation may provide multiple investment management services, in which case the service auditor identifies how the services interface.
62. ~~CG2~~~~C3~~~~CG4~~In assessing the reasonableness of the control objectives,⁵⁰ the service auditor determines whether the control objectives for the relevant investment management service/s contained in Appendix 3 have been included or, for any objectives which have been excluded, the adequacy of the reasons why those objectives are not relevant. If there are any unjustified omissions or misstatements with regard to the control objectives, the service auditor asks management, or those charged with governance, to amend the description. If it is not amended, the service auditor considers the reasons, if known, for the omission or misstatement and the effect on the Service Auditor's Type 1 or 2 Report.

⁴⁹ See ASAE 3402, paragraph 20.

⁵⁰ See ASAE 3402, paragraph 21.

Conducting the Assurance Engagement to Report on Controls

63. The service auditor complies with the requirements of ASAE 3402 when conducting an assurance engagement to report on controls at the service organisation when:
- (a) obtaining evidence regarding the description, design and operating effectiveness of controls;⁵¹
 - (b) considering the work of an internal audit function;⁵²
 - (c) obtaining written representations from the service organisation;⁵³
 - (d) considering other information;⁵⁴
 - (e) enquiring and, if necessary, disclosing subsequent events;⁵⁵ and
 - (f) preparing and assembling documentation.⁵⁶

The Service Auditor's Assurance Report

64. The service auditor's opinion is expressed in a written assurance report on controls attached to the service organisation's description of its system and assertion.
65. The Service Auditor's Type 1 or 2 Report, includes the basic elements required by ASAE 3402⁵⁷ with specific consideration of matters relevant to investment management services, including:
- (a) A statement that the criteria include the minimum control objectives provided in this guidance statement for the relevant investment management services; and

⁵¹ See ASAE 3402 paragraphs 21-29.
⁵² See ASAE 3402 paragraphs 30-37.
⁵³ See ASAE 3402 paragraphs 38-40.
⁵⁴ See ASAE 3402 paragraphs 41-42.
⁵⁵ See ASAE 3402 paragraphs 43-44.
⁵⁶ See ASAE 3402 paragraphs 45-52.
⁵⁷ See ASAE 3402, paragraph 53.

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- (b) A statement that the service organisation is responsible for:
 - (i) Providing the investment management services covered by the service organisation's description of its system; and
 - (ii) Stating the control objectives, including those for the relevant investment management services from this guidance statement, and if any minimum control objectives are omitted or modified providing an explanation of that omission or modification.

An example of a service auditor's type 2 report is shown at Appendix 4.

Describing Tests of Operating Effectiveness

66. The Service Auditor's Type 2 Report includes a separate attachment that describes the service auditor's tests of controls and the results thereof. An explanation of the service auditor's description of the nature, timing and extent of tests applied to controls is in Appendix 5.

~~CG5~~/CG6 Modified Opinions

67. When preparing the assurance report, the service auditor is required to modify their opinion in the circumstances set out in ASAE 3402.⁵⁸ If the service auditor concludes that the control objectives for the investment management services are incomplete and the service organisation refuses to amend their report to address those control objectives, the service auditor may modify their opinion if it has a material impact on the fair presentation of the description.

Other Communication Responsibilities

68. ASAE 3402⁵⁹ requires the service auditor to determine whether non-compliance with laws and regulations, fraud, or uncorrected errors

⁵⁸ See ASAE 3402 paragraph 55.

⁵⁹ See ASAE 3402 paragraph 56.

which are not clearly trivial, have been communicated to affected user entities and, if not, to take appropriate action.

Service Auditor Engagements to report on financial information

69. If the service auditor is engaged to provide a report on financial information, the service auditor issues a separate auditor's report in respect of each user entity concerning only that user entity's balances and/or transactions.
70. In performing an engagement to report on specified assertions or on a Statement the service auditor applies the Auditing Standards (ASAs) and reports on the engagement under ASA 805.
71. If the service auditor has prepared a Type 2 Report it provides the service auditor with assurance as to the reliability of controls over the investment management services which relate to the user entity's balances and/or transactions. Accordingly the service auditor may be able to reduce the extent of substantive testing that might otherwise be necessary in preparing a Service Auditor's Report on financial information.

Acceptance and Continuance of an Audit Engagement

72. Before accepting the engagement, the service auditor is required under ASA 210⁶⁰ to determine the acceptability of the financial reporting framework, which in the case of a single financial statement or element, includes determining whether application of the financial reporting framework will result in a presentation that provides adequate disclosures to enable the intended users to understand the information conveyed and the effect of material transactions and events on the information conveyed.⁶¹
73. The service auditor also complies with Auditing Standard ASA 210 in agreeing the terms of engagement.⁶² In addition to the matters specified in ASA 210, the engagement letter or other written

⁶⁰ See ASA 210 *Agreeing the Terms of Audit Engagements*, paragraph 6(a).

⁶¹ See ASA 805, paragraph 8.

⁶² See ASA 210, paragraphs 9 & 10.

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agreement between the service auditor and the service organisation may include:

- The service auditor's responsibility to conduct the engagement with reference to this Guidance Statement.
- The service auditor's responsibility to report, in an attachment to the Service Auditor's Report, uncorrected misstatements which have been aggregated during the audit, other than amounts which are clearly trivial.
- Reference to the performance materiality level provided by the user auditor, if applicable.

Example engagement letters for engagements to report on specified assertions and on a Statement are included in Appendix 1 Examples 2 and 3 respectively.

Ethical Requirements

74. In accordance with Auditing Standard ASA 200,⁶³ the service auditor is required to comply with relevant ethical requirements, including those pertaining to independence, when performing an audit of a Statement or specified assertions. Relevant ethical requirements are defined in ASA 102.⁶⁴
75. The service auditor considers the fundamental principles of professional ethics, relating to the engagement to be undertaken, which include:⁶⁵
- (a) integrity;
 - (b) objectivity;
 - (c) professional competence and due care;

⁶³ See ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.

⁶⁴ See Complied ASA 102 *Compliance with Ethical Requirements when Performing Audits, Reviews and Other Assurance Engagements*.

⁶⁵ See ASA 102, paragraph A3.

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- (d) confidentiality; and
 - (e) professional behaviour.
76. Where the service auditor is undertaking an audit of a Statement or specified assertion particular consideration needs to be given to any threats to independence with respect to the user entity since the service auditor is reporting on financial information of the user entity. Threats to independence with respect to the user entity may be present, such as self-interest or familiarity threats, notwithstanding that the user entity may not be an assurance client of the service auditor.
77. In evaluating threats to independence and considering applicable safeguards, the service auditor considers the nature of the engagement. It may be sufficient, for example in the case of a restricted use report, to apply independence requirements in evaluating the independence of the engagement team members and their immediate and close family with respect to the user entity, along with limited consideration of the firm's interests and relationships with the user entity.
78. Examples of safeguards that may be considered appropriate by service auditors to manage identified threats to independence include:
- Prohibiting the holding of direct, or material indirect, financial interests in the user entity or its affiliates by members of the service auditor's engagement team and their immediate and close family.
 - Removal from the service auditor's engagement team of any personnel with a close relationship with directors, officers or employees of the user entity or its affiliates.

Materiality to be Applied by the Service Auditor

79. When conducting an audit of specified assertions or a Statement, the service auditor considers materiality under ASA 320 in determining the nature, timing and extent of audit procedures and evaluating the

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effect of misstatements. The relevant benchmark, for investment management services, on which the service auditor bases materiality, under ASA 320, in most cases is either:

- (a) the assets of the user entity for which specific assertions are being audited;
- (b) total assets of the user entity reported in the Statement; or
- (c) net assets, where assets and liabilities are reported, of the user entity reported in the Statement.

80. The service auditor often applies a percentage to the benchmark as a starting point in determining materiality under ASA 320.⁶⁶ In the absence of a materiality specified by the user auditor, the service auditor may apply a percentage of 0.5% to any of the benchmarks listed in paragraph 79 as a reasonable basis for determining performance materiality for auditing specified assertions or a Statement, where investment management services are provided. Where an alternative benchmark is used, this percentage may not be appropriate for determining materiality.

81. If the user auditor requests that an alternative benchmark or percentage be used as a basis for determination of performance materiality to be applied by the service auditor, then this is communicated by the user entity to the service organisation and agreed between the service organisation and the service auditor.

Service Auditor's Reports on Financial Information

82. Service Auditor's Reports on Specified Assertions or on a Statement, need to comply with the requirements in ASA 805 and as such include the basic elements of an Auditor's Report as set out in that standard. In addition to these elements, the service auditor includes in their report:

- (a) identification of the specific assertions audited (if report is limited to specific assertions);

⁶⁶ See ASA 320, paragraph A3.

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- (b) identification of the investment management services provided by the service organisation to the user entity;
- (c) a description of the responsible party's (management, or those charged with governance, of the service organisation) responsibilities for the investment management services provided to the user entity;
- (d) reference to the contract or service level agreement between the service organisation and the user entity for the investment management services provided; and
- (e) reference to the use of the report by the user entity and the user auditor.

Examples of a Service Auditor's Report on Specified Assertions is provided in Appendix 6 Example 1 and a Service Auditor's Report on a Statement is provided in Appendix 6 Example 2 of this Guidance Statement.

Information Excluded from the Service Auditor's Report

83. When performing an audit engagement at a service organisation, the service auditor may restrict the audit procedures to information that is held by the service organisation on behalf of the user entity. The Statement, however, may include information which is provided by the fiduciary of the user entity or by another party to the service organisation for inclusion in the Statement. Documentation or other audit evidence may not be available at the service organisation to substantiate that information. Where certain information within the Statement has not been audited, the service auditor identifies that information and specifically excludes it from the scope of the audit opinion.

Reporting of Matters of Governance Interest Arising in an Audit Engagement on Financial Information

84. In the course of performing procedures for an audit engagement at a service organisation, the service auditor is required to communicate any of the following matters identified to those charged with governance on a timely basis:

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- (a) significant deficiencies in internal control;⁶⁷
 - (b) significant findings from the audit;⁶⁸
 - (c) uncorrected misstatements and the effect they, individually or in aggregate, may have on the opinion in the auditor's report;⁶⁹ and
 - (d) fraud, identified or suspected involving management, employees who have significant roles in internal control or others where the fraud results in a material misstatement, as well as any other matters related to fraud that are relevant to their responsibilities.⁷⁰
85. In addition, the service auditor states in their report whether they have identified any uncorrected misstatements in the course of the audit, other than amounts which are clearly trivial, and, if so, details the uncorrected misstatements in an attachment to their report. An outline for an attachment on uncorrected misstatements is shown at Appendix 6, Example 2.
86. If the service auditor considers that any of the matters reported to those charged with governance of the service organisation may affect one or more user entity, the service auditor determines from the appropriate level of management whether this information has been communicated to the affected user entity or entities. If the matter is not communicated satisfactorily, the service auditor may consider whether it affects the service auditor's ability to conduct the engagement or necessitates a modification to the service auditor's report.

⁶⁷ See ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*, paragraph 9.

⁶⁸ See ASA 260 *Communication with Those Charged with Governance*, paragraph 16.

⁶⁹ See ASA 450 *Evaluation of Misstatements Identified during the Audit* paragraph 12.

⁷⁰ See ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*, paragraph 41 and 42.

Conformity with International Pronouncements

87. There is no equivalent International Standard on Auditing or International Practice Statement to this Guidance Statement.

Draft

Appendix 1

(Ref: Para. 50 & 73)

ENGAGEMENT LETTERS

The following example engagement letters are not authoritative but are intended only to be a guide that may be used in conjunction with the considerations outlined in GS 007. The engagement letters will need to be varied according to individual requirements and circumstances. It is drafted to refer to an engagement for a single reporting period and would require adaptation if intended or expected to apply to recurring engagements.⁷¹ It may be appropriate to seek legal advice that any proposed letter is suitable.

Example 1: Example Engagement Letter for a Type 2 Report on a Service Organisation's Controls

To [the appropriate representative of management or those charged with governance] of XYZ Service Organisation (XYZ):

[The objective and scope of the engagement]

You have requested that we report on the description of XYZ's [investment management service provided: custody; asset management, property management, superannuation member administration, investment administration or registry] system and management's assertion with respect to that description, which you will provide and which will accompany our report. The description of XYZ's [investment management service] system comprises control objectives and related controls designed to achieve those objectives for the period ended [date]. The control objectives included are the objectives for [investment management service] specified in Guidance Statement GS 007⁷² and any additional objectives which are likely to be relevant to internal control as it relates to financial reporting of clients who have used the [investment management service] system.

We are pleased to confirm our acceptance and understanding of this engagement by means of this letter. Our engagement will be conducted with

⁷¹ See ASA 210, paragraph 13.

⁷² See GS 007 Appendix 4.

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Appendix 1, Example 1

the objective of our expressing an opinion on the fair presentation of the [investment management service] system, suitability of the design of the controls to achieve the control objectives throughout the period and the operating effectiveness of the controls necessary to provide reasonable assurance that the control objectives were achieved throughout the period.

[The responsibilities of the assurance practitioner]

We will conduct our assurance engagement in accordance with Standard on Assurance Engagements ASAE 3402 *Assurance Reports on Controls at a Service Organisation* and with reference to Guidance Statement GS 007 *Audit Implications of the Use of Service Organisations for Investment Management Services*. ASAE 3402 requires that we comply with ethical requirements and plan and perform procedures to obtain reasonable assurance about whether, in all material respects, XYZ's description of the [investment management service] system is fairly presented, the controls are suitably designed, and operating effectively throughout the reporting period. An assurance engagement involves performing procedures to obtain evidence about the description, design and operating effectiveness of controls. The procedures selected depend on the assurance practitioner's judgement, including the assessment of the risks of significant deficiencies in the [investment management service] system.

Because of the inherent limitations of an assurance engagement, together with the inherent limitations of any internal control system there is an unavoidable risk that some significant deficiencies may not be detected, even though the engagement is properly planned and performed in accordance with Standards on Assurance Engagements.

The system, within which the controls that we will test operate, will not be examined except to the extent the system is likely to be relevant to clients, as it relates to financial reporting. Hence no opinion will be expressed as to the effectiveness of the internal control system as a whole.

The work undertaken by us to form an opinion, is permeated by judgement, in particular regarding the nature, timing and extent of assurance procedures for gathering evidence and the drawing of conclusions based on the evidence gathered. In addition to the inherent limitations in any assurance

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Appendix 1, Example 1

engagement, which include the use of testing, inherent limitations of any internal control structure, and the possibility of collusion, most evidence is persuasive rather than conclusive. As a result, an assurance engagement can only provide reasonable – not absolute – assurance that the description is fairly presented, controls are suitably designed and controls have operated effectively throughout the period.

[The responsibilities of Management and identification of the applicable control framework]

Our assurance engagement will be conducted on the basis that [management or, where appropriate, those charged with governance] acknowledge and understand that they have responsibility:

- (a) For the preparation of a written assertion that, in all material respects, and based on suitable criteria:
 - (i) the description fairly presents the XYZ's [investment management service] system designed and implemented throughout the period;
 - (ii) The controls related to the control objectives stated in XYZ's description of its system were suitably designed throughout the specified period;
 - (iii) The controls related to the control objectives stated in XYZ's description of its system operated effectively throughout the specified period.
- (b) For design of the system, comprising controls which will achieve control objectives which are likely to be relevant to clients', who have used [investment management service] system, internal control as it relates to financial reporting;
- (c) To provide us with:
 - (i) Access to all information of which those charged with governance and management are aware that is relevant to

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Appendix 1, Example 1

- the design, implementation and operation of the [investment management service] system;
- (ii) Additional information that we may request from those charged with governance and management for the purposes of this assurance engagement; and
 - (iii) Unrestricted access to persons within the entity from whom we determine it necessary to obtain evidence.

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

XYZ's description of the system will include the control objectives for [investment management service] set out in GS 007, but they may add to these to the extent that the control objectives are likely to be relevant to clients', who have used [investment management service] system, internal control as it relates to financial reporting. If [management/those charged with governance] consider any of the control objectives from GS 007 for [investment management service] are not applicable to XYZ, then they will include an explanation of the omission of that objective in XYZ's description of the system.

[Assurance Approach]

We will examine and evaluate the control objectives and controls for [investment management service] system described above. The "Description of [investment management service] System" will include details of controls with which clients should comply. While our evaluation will include assessment of the appropriateness of the complementary client controls, our testing will not encompass evaluation of the suitability of design or operating effectiveness of controls carried out by users of XYZ's [investment management service] system. The control objectives stated in XYZ's description of its system can be achieved only if complementary user entity controls are suitably designed or operating effectively, along with the controls at the service organisation.

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Appendix 1, Example 1

Our procedures will extend to the control objectives and related controls at relevant subservice organisations only to the extent that those controls are included in XYZ's description of [investment management service] system and are necessary to achieve the relevant control objectives.

Due to the complex nature of internal control, our assurance procedures will not encompass all individual controls at XYZ, but will be restricted to an examination of those controls reported which achieve the control objectives identified by XYZ's management in the "Description of the [investment management service] System" provided to us.

[Assurance Procedures]

Our assurance procedures are likely to include:

1. Performing a preliminary review of the control environment of XYZ relevant to the [investment management service] system;
2. Evaluating the reasonableness of the control objectives against the minimum objectives for [investment management service] provided in GS 007;
3. Evaluating the completeness, accuracy and presentation of the Description of the [investment management service] System against the controls implemented.
4. Evaluating the design of specific controls by:
 - (i) Assessing the risks that threaten the achievement of the control objectives.
 - (ii) Evaluating whether the controls described are capable of addressing those risks and achieving the related objectives.
5. Performing tests of controls to ascertain whether the degree of compliance with controls is sufficient to provide reasonable assurance that the controls have achieved their objectives throughout the period.

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In undertaking this engagement, we shall work closely with XYZ's internal audit function and place reliance on their work in accordance with ASA 610 *Using the Work of Internal Auditors* [this paragraph is applicable where the work of internal audit is an integral part of the assurance engagement].

[Assurance Report]

The format of the report will be in accordance with ASAE 3402 and will include an opinion on the "Description of the [investment management service] System" by XYZ management and an accompanying description of the tests of controls that we performed and the results of those tests. An example of the proposed report is contained in the appendix to this letter.

Our report will be issued [frequency] and will cover [period reported on] (paragraph is appropriate for recurring engagements).

The assurance report will be incorporated in a report issued by the XYZ containing information prepared by XYZ management to provide to clients and their auditors with an overall understanding of [subject matter]. We will review the contents of the report issued by XYZ to identify any material inconsistencies with the Description of the [investment management service] System.

[Distribution of the Assurance Report]

Our report and the accompanying description of tests of controls are intended only for clients of XYZ which use the [investment management service] system and their auditors, who have a sufficient understanding to consider it, along with other information including information about controls operated by clients themselves, when assessing the risks of material misstatements of clients' financial reports.

Our assurance report will be prepared for this purpose only and we disclaim any assumption of responsibility for any reliance on our report to any person

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other than to XYZ's clients and their auditors or for any purpose other than that for which it was prepared.⁷³

[Significant Deficiencies in Controls]

We will issue an assurance report without modification, to provide reasonable assurance on the [investment management service] system where our procedures do not disclose a significant deficiency in the controls necessary to achieve the control objectives contained in the Description of the [investment management service] System by XYZ management. For this purpose, a significant deficiency exists when prescribed control procedures, or the degree of compliance with them:

- (a) does not provide XYZ management with reasonable assurance that the control objectives will be met or that fraud, error, or non-compliance with laws and regulations would be prevented or detected by employees in the normal course of their assigned functions; and
- (b) knowledge of that deficiency would be material to users of the assurance report.

If our assurance engagement discloses that there are significant deficiencies in the system of controls in operation during the period covered by the report, such deficiencies will be disclosed in our report even if they were corrected prior to the end of the reporting period. However, our report will indicate that such deficiencies were corrected if that is the case. If any significant deficiencies disclosed in our report have been corrected subsequent to this period (or are in the process of being corrected), we will refer to this in our report.

Although the primary purpose of our assurance engagement will be to enable us to issue the above described report, will also periodically provide you with letters containing recommendations for strengthening controls if such matters

⁷³ Use of the report & liability limitation: insert additional wording, if any, required to reflect any liability arrangements agreed between the service auditor, the service organisation and other users, including confirmation of the purpose for which the service auditor's report has been prepared and the basis on which other parties may use the report.

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are observed during the process of the assurance engagement. Although issues raised may not represent significant deficiencies in the system of controls, recommendations will address areas where we believe controls could be improved.

We look forward to full co-operation from your staff during our assurance engagement.

[Other relevant information]

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

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our assurance engagement to report on the control procedures over XYZ's [investment management service] services to clients, including our respective responsibilities.

Yours faithfully,

(signed)

.....

Name and Title

Date

Acknowledged on behalf of XYZ

(signed)

.....

Name and Title

Date

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Appendix 1

Example 2: Example Engagement Letter for an Audit of Specified Assertions

To [the appropriate representative of management or those charged with governance] of the XYZ Service Organisation (XYZ):⁷⁴

[The objective and scope of the audit]

You⁷⁵ have requested that we audit the [specify assertions audited: for transactions or events: occurrence, completeness, accuracy, cut-off and classification; for balances: existence, rights and obligations, completeness or valuation and allocation; or for presentation and disclosure: occurrence, rights and obligations, completeness, classification and understandability and accuracy and valuation] of the assets [and liabilities or transactions] in the [title of the financial statement] of [user entity/entities] ("the Statement"), which comprises the [statement of assets and liabilities] as at [date], and the [statement of transactions] for the [period] then ended, concerning the assets and liabilities of [user entity/ies]⁷⁶ [nature of investment management service: managed by or in the custody] of XYZ as at [date].

We are pleased to confirm our acceptance and our understanding of this engagement by means of this letter. Our audit will be conducted with the objective of our expressing an opinion on the [specify assertions audited: existence, rights and obligations, completeness or valuation & allocation] of the assets [and liabilities or transactions] in the Statement.

⁷⁴ 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 ASA 210 Paragraph A21.

⁷⁵ 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.

⁷⁶ Where the assets are held in the name of a nominee holding company insert "held in the name of [nominee holding company]".

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[The responsibilities of the auditor]

We will conduct our audit in accordance with the Australian Auditing Standards, in particular ASA 805 *Special Considerations – Audit of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement*, and with reference to GS 007 *Audit Implications of the Use of Service Organisations for Investment Management Services*. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the Statement is free from material misstatement with respect to the assertions specified. This audit involves performing procedures to obtain audit evidence about the [specify assertions audited: existence, rights and obligations, completeness or valuation & allocation] of the assets [and liabilities or transactions] in the Statement. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement with respect to the [specify assertions audited: existence, rights and obligations, completeness or valuation & allocation] of the assets [and liabilities or transactions] in the Statement, whether due to fraud or error. An audit also includes evaluating the appropriateness of the financial reporting framework, accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the presentation of the Statement with respect to the [specify assertions audited] of the assets [and liabilities or transactions] in the Statement.

Because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that even 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 XYZ's preparation of the Statement in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an

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Appendix 1, Example 2

opinion on the effectiveness of XYZ's controls.⁷⁷ However, we will communicate to you in writing concerning any significant deficiencies in internal controls over financial reporting on behalf of [user entity/ies], that we have identified during the audit of the [specify assertions audited] of the assets [and liabilities or transactions] in the Statement.

We will report any uncorrected misstatements which we have aggregated during the audit but that were determined by management to be immaterial, both individually and in aggregate, to the Statement taken as a whole, other than amounts which are clearly trivial, in an attachment to our report.

[The responsibilities of management and identification of the applicable financial reporting framework]

Our audit will be conducted on the basis that management and, where appropriate, those charged with governance,⁷⁸ acknowledge and understand that they have responsibility:

- (a) For such internal control as [management] determines is necessary to enable the preparation of a Statement that is free from misstatement, whether due to fraud or error;
- (b) To provide us with:
 - (i) Access to all information of which those charged with governance and management are aware that is relevant to the preparation of the Statement such as records, documentation and other matters;

⁷⁷ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the Statement, this sentence would be worded as follows: "In making those risk assessments, the auditor considers internal control relevant to [name of service organisation]'s preparation and fair presentation of the Statement in order to design audit procedures that are appropriate in the circumstances."

⁷⁸ 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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- (ii) Additional information that we may request from those charged with governance 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.

[Distribution of the Auditor's Report]

We understand that our report may be incorporated in a report prepared by XYZ for distribution to the [Trustee/those charged with governance] of [user entity] for the purpose of fulfilling the [those charged with governance] of XYZ's reporting obligations under the [title of contract or service level agreement]. Our report will be prepared for this purpose only and we disclaim any assumption of responsibility for any reliance on our report, or on the Statement to which it relates, to any person other than [those charged with governance] of XYZ, [the Trustee/those charged with governance] of [client] and their Auditor, or for any other purpose other than that for which it was prepared.⁷⁹

[Other relevant information]

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

⁷⁹ Use of the report & liability limitation: insert additional wording, if any, required to reflect any liability arrangements agreed between the service auditor, the service organisation and other users, including confirmation of the purpose for which the service auditor's report has been prepared and the basis on which other parties may use the report.

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[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.

[Independence]

We confirm that, to the best of our knowledge and belief, the engagement team are independent of [user entity / user entities] in accordance with [specify relevant ethical requirements] in relation to the audit of the [specify assertions audited] of the assets [and liabilities or transactions] in the Statement. In conducting our audit of the [specify assertions audited] of the assets [and liabilities or transactions] in the Statement, should we become aware that we are not in compliance with the independence requirements of [specify relevant ethical requirements] we shall notify you on a timely basis.

Please sign and return the attached copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our audit of [specify assertions audited] of the assets [and liabilities or transactions] in the Statement including our respective responsibilities

Yours faithfully,

(signed)

.....

Partner

Firm

Acknowledged and agreed on behalf of XYZ by (signed)

.....

Name and Title

Date

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Example 3: Engagement Letter for an Audit of a Statement

To the appropriate representative of management or those charged with governance of the XYZ Service Organisation (XYZ).⁸⁰

[The objective and scope of the audit]

You⁸¹ have requested that we audit the [title of financial statement] of [user entity/ies]⁸² (“the Statement”), which comprises the [statement of assets and liabilities] as at [date], and the [statement of transactions] for the year then ended, concerning the assets [and liabilities or transactions] of [user entity/ies]⁸³ [insert nature of investment management service: managed by or in the custody of] XYZ as at [date].

We are pleased to confirm our acceptance and our understanding of this engagement by means of this letter. Our audit will be conducted with the objective of our expressing an opinion on the Statement.

[The responsibilities of the auditor]

We will conduct our audit in accordance with the Australian Auditing Standards, in particular ASA 805 *Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement*, and with reference to GS 007 *Audit Implications of the Use of Service Organisations for Investment Management Services*. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the Statement is free from material misstatement. [If the user auditor has provided a materiality level to apply in the audit insert: The performance materiality level, which we will apply in determining the nature, timing and extent of audit procedures and in evaluating the effect of misstatements identified, has

⁸⁰ 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 ASA 210 Paragraph A21.

⁸¹ 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.

⁸² If certain assertions are specifically excluded from the audit then insert: “except for [specify assertions excluded, e.g. presentation & disclosure] of the Statement”.

⁸³ Where the assets are held in the name of a nominee holding company insert “held in the name of [nominee holding company]”.

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been provided by the auditor of [user entity] and is [x] percent of [total assets/net assets]. This audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Statement. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the Statement, whether due to fraud or error. An audit also includes evaluating the appropriateness of the financial reporting framework, accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the Statement.

Because of the other inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that even material misstatements 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 XYZ's preparation of the Statement 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 XYZ's controls.⁸⁴ However, we will communicate to you in writing concerning any significant deficiencies in internal controls over financial reporting on behalf of [user entity], that we have identified during the audit of the Statement.

We will report any uncorrected misstatements which we have aggregated during the audit but that were determined by management to be immaterial, both individually and in aggregate, to the Statement taken as a whole, other than amounts which are clearly trivial, in an attachment to our report.

⁸⁴ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the Statement, this sentence would be worded as follows: "In making those risk assessments, the auditor considers internal control relevant to [name of service organisation]'s preparation and fair presentation of the Statement in order to design audit procedures that are appropriate in the circumstances."

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Appendix 1, Example 3

[The responsibilities of management and identification of the applicable financial reporting framework]

Our audit will be conducted on the basis that [management and, where appropriate, those charged with governance]⁸⁵ acknowledge and understand that they have responsibility:

- (a) for the preparation of the Statement that gives a true and fair view in accordance with [specify framework].⁸⁶
- (b) For such internal control as [management] determines is necessary to enable the preparation of a Statement that is free from misstatement, whether due to fraud or error.
- (c) To provide us with:
 - (i) Access to all information of which those charged with governance and management are aware that is relevant to the preparation of the Statement such as records, documentation and other matters;
 - (ii) Additional information that we may request from which those charged with governance 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, from 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.

⁸⁵ Use terminology as appropriate in the circumstances.

⁸⁶ Insert "applicable Australian Accounting Standards" where multiple Australian Accounting Standards were applied; insert reference to a specific Australian Accounting Standard where appropriate (for example: "the measurement standards of AAS 25 Financial Reporting by Superannuation Plans."); or "the accounting policies described in Note X to the Statement".

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[Distribution of the Auditor's Report]

We understand that our report may be incorporated in a report prepared by XYZ for distribution to the [Trustee/those charged with governance] of [user entity] for the purpose of fulfilling the [those charged with governance] of XYZ's reporting obligations under the [title of contract or service level agreement]. Our report will be prepared for this purpose only and we disclaim any assumption of responsibility for any reliance on our report, or on the Statement to which it relates, to any person other than [those charged with governance] of XYZ, [the Trustee/those charged with governance] of [client] and their Auditor, or for any other purpose other than that for which it was prepared.⁸⁷

[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.

[Independence]

We confirm that, to the best of our knowledge and belief, the engagement team is independent of [user entity/user entities] in accordance with [specify relevant ethical requirements] in relation to the audit of the Statement. In conducting our audit of the Statement, should we become aware that we have contravened the independence requirements of [specify relevant ethical requirements] we shall notify you on a timely basis.

⁸⁷ Use of the report & liability limitation: insert additional wording, if any, required to reflect any liability arrangements agreed between the service auditor, the service organisation and other users, including confirmation of the purpose for which the service auditor's report has been prepared and the basis on which other parties may use the report.

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

Yours faithfully,

(signed)

.....

Partner

Firm

Acknowledged and agreed on behalf of [XYZ] by

(signed)

.....

Name and Title

Date

Appendix 2

(Ref: para. 57)

SERVICE ORGANISATION'S TYPE 2 CONTROLS ASSERTION AND DESCRIPTION OF THE SYSTEM

The following example is for use as a guide only, in conjunction with the considerations described in GS 007, and are not intended to be exhaustive or applicable to all situations.

XYZ Service Organisation's Type 2 Assertion on the [Investment Management Service] System

Assertion by XYZ Service Organisation

The accompanying description has been prepared for clients who have used the [investment management service] system and their auditors who have a sufficient understanding to consider the description, along with other information including information about controls operated by clients themselves, when assessing the risks of material misstatements of clients' financial reports/statements. XYZ Service Organisation confirms that:

- (a) The accompanying description at pages [bb-cc] fairly presents the [investment management service] system for processing clients' transactions throughout the period [date] to [date]. The criteria used in making this assertion were that the accompanying description:
- (i) Presents how the system was designed and implemented, including:
- The types of services provided, including, as appropriate, classes of transactions processed.
 - The procedures, within both information technology and manual systems, by which those transactions were initiated, recorded, processed, corrected as necessary, and transferred to the reports prepared for clients.

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- The related accounting records, supporting information and specific accounts that were used to initiate, record, process and report transactions; this includes the correction of incorrect information and how information was transferred to the reports prepared for clients.
- How the system dealt with significant events and conditions, other than transactions.
- The process used to prepare reports for clients.
- Relevant control objectives and controls designed to achieve those objectives, including the control objectives for [investment management service] provided in *Guidance Statement 007 Audit Implications of the Use of Service Organisations for Investment Management Services* except for [number excluded] control objectives for the reasons set out in the attached Description of Controls in Operation.⁸⁸
- Controls that we assumed, in the design of the system, would be implemented by clients, and which, if necessary to achieve control objectives stated in the accompanying description, are identified in the description along with the specific control objectives that cannot be achieved by ourselves alone.
- Other aspects of our control environment, risk assessment process, information system (including the related business processes) and communication, control activities and monitoring

⁸⁸ Insert if certain control objectives specified in this Guidance Statement are not met by relevant controls.

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controls that were relevant to processing and reporting clients' transactions.

- (ii) Includes relevant details of changes to the service organisation's system during the period [date] to [date].
 - (iii) Does not omit or distort information relevant to the scope of the system being described, while acknowledging that the description is prepared to meet the common needs of a broad range of clients and their auditors and may not, therefore, include every aspect of the system that each individual client may consider important in its own particular environment.
- (b) The controls related to the control objectives stated in the accompanying description were suitably designed and operated effectively throughout the period [date] to [date]. The criteria used in making this assertion were that:
- (i) The risks that threatened achievement of the control objectives stated in the description were identified;
 - (ii) The identified controls would, if operated as described, provide reasonable assurance that those risks did not prevent the stated control objectives from being achieved; and
 - (iii) The controls were consistently applied as designed, including that manual controls were applied by individuals who have the appropriate competence and authority, throughout the period [date] to [date].

.....

Signed on behalf of [Management/Those Charged with Governance] of XYZ Service Organisation

Date

Appendix 2

ATTACHMENT 1: XYZ Service Organisation's Description of the [Investment Management Service] System Accompanying XYZ Service Organisation Management's Assertion

XYZ Service Organisation's [Investment Management Service] System

Services Provided

XYZ Service Organisation (XYZ) provides its clients with [investment management service/s: custody, asset management, property management, superannuation member administration, investment administration or registry] services, which involves [describe services provided].

The System

The stated internal control objectives and related controls included in this report apply to XYZ operations as they relate only to [investment management service] services. Specifically excluded from this report are controls within individual systems, controls executed at client premises and other services provided by XYZ, including [other related services provided to clients].

The effectiveness of controls performed by clients of XYZ should also be considered as part of the overall system of control relating to XYZ's [investment management service] services.

[Describe, as appropriate:⁸⁹

- *The procedures, within both information technology and manual systems, by which those transactions were initiated, recorded, processed, corrected as necessary, and transferred to the reports prepared for clients.*

⁸⁹ Aspects of the system to be described here relate to the manner in which the system operates to provide services to clients but do not include specific controls which are designed to achieve the control objectives.

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- *The related accounting records, supporting information and specific accounts that were used to initiate, record, process and report transactions; this includes the correction of incorrect information and how information is transferred to the reports prepared for clients.*
- *How the system dealt with significant events and conditions, other than transactions.*
- *The process used to prepare reports for clients.*

This may include a description of the flow of transactions or a flowchart].

[Controls at Subservice Organisations]⁹⁰

[XYZ uses [name of subservice organisation] to provide [type or name of] services, which form part of the [investment management service] system used by XYZ clients. The [type or name of] services provided by [subservice organisation] are [describe the nature of the services provided]. XYZ's description of the system includes XYZ's monitoring controls over the operating effectiveness of the controls at [subservice organisation] and [includes/excludes]⁹¹ the relevant control objectives and related controls of [subservice organisation].

Internal Control Objectives and Related Controls

We set out in this report the control objectives and related controls implemented for XYZ. The specific controls set out in the remainder of the report have been designed to achieve each of the control objectives. The controls have been in place throughout the period from [date] to [date] unless otherwise indicated.

The Controls which were in operation at XYZ throughout the period from [date] to [date], or during a lesser period where specified, to ensure that the

⁹⁰ Insert this section if XYZ Service Organisation uses a subservice organisation which performs some of the services provided to clients which use the system.

⁹¹ Use "includes" if the inclusive method is used and "excludes" if the carve-out method is used with respect to the subservice organisation's services.

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identified Control Objectives over [investment management service] are achieved were:

Internal Control Objective

[Control objectives, including those for the relevant investment management service/s from GS 007 Appendix 3.]⁹²

Related Controls

[List controls in operation during the specified period relating to each control objective]

*[**Period of operation:** If the control has not been in operation the entire period or has changed, state the period during which the control was operating and the period during which the change was effective.]⁹³*

*[**Complementary client controls:** Describe any complementary user entity controls contemplated in the design of the controls.]⁹⁴*

[The description may be presented in various formats such as narratives, flowcharts, tables or graphics, with an indication of the extent of manual and computer processing used.]

⁹² Where the control objective is excluded from the system description, insert: "This control objective is not relevant to the operation of [service organisation]'s [investment management service] services because [specify reasons] and so has not been addressed by related controls."

⁹³ This section should be inserted for each control which has not been in operation for the whole period or has changed during the period.

⁹⁴ This section should be inserted for each control for which there are complementary user entity controls contemplated in the design of the control.

Appendix 3

(Ref: para 48)

MINIMUM CONTROL OBJECTIVES FOR EACH INVESTMENT MANAGEMENT SERVICE

This section sets out detailed control objectives for the investment management services referred to in GS 007 paragraph 12 and further defined below. The control objectives listed are the minimum objectives which the service auditor and users of a Type 1 or 2 Report may reasonably expect to be addressed in the service organisation's description of its investment management services system, but are not intended to be exhaustive. The control objectives included are those which are likely to be relevant to user entities' controls as they relate to financial reporting and not for other purposes, such as to meet compliance requirements or to assess performance with respect to service level agreements. It remains the responsibility of management, or those charged with governance, of the service organisation to ensure that the described control objectives are likely to be relevant to client's controls as they relate to financial reporting. However control objectives for other purposes may be included if the service organisation requires those objectives to be addressed in the engagement.

A. Custody

Definition:

"Custody" is the performance of the following functions on behalf of user entities:

- Maintaining custody of assets and records of the assets held for user entities (Such assets may exist in physical or electronic form).
- Collecting income and distributing such income to user entities.
- Receiving notification of corporate events and reflecting such events in the records of user entities.

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- Receiving notification of asset purchase and sale transactions on behalf of user entities for which the custodian is holding assets, and reflecting such transaction in the records of user entities.
- Receiving payments from purchasers and disbursing proceeds to sellers for asset purchase and sale transactions.

Control Objectives:

Accepting clients

- A1.** Accounts are set up completely and accurately in accordance with client agreements and applicable regulation.
- A2.** Complete and authorised client agreements are established prior to initiating custody activity.
- A3.** Investment holdings and related history (where applicable) transferred from prior custodians are received and recorded completely, accurately and on a timely basis.

Authorising and processing transactions

- A4.** Investment and related cash and foreign exchange transactions are authorised and recorded completely, accurately and on a timely basis in accordance with client instructions.
- A5.** Investment and related cash and foreign exchange transactions are settled completely, accurately and on a timely basis and failures are resolved in a timely manner.
- A6.** Corporate events and voting instructions are identified, actioned, processed and recorded on a timely basis.
- A7.** Cash receipts and payments are authorised, processed and recorded completely, accurately and on a timely basis.

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- A8.** Securities lending programs are authorised and loan initiation, maintenance and termination are recorded on an accurate and timely basis.
- A9.** Loans are collateralised in accordance with the lender's agreement and the collateral together with its related income is recorded completely, accurately and on a timely basis.
- A10.** Collateral is completely and accurately invested in accordance with the lender's agreement.

Maintaining financial and other records

- A11.** Accounts are administered in accordance with client agreements and applicable regulations.
- A12.** Changes to non-monetary static data (for example, address changes and changes in allocation instructions) are authorised and correctly recorded on a timely basis.
- A13.** Investment income and related tax reclaims are collected and recorded accurately and on a timely basis.
- A14.** Asset positions for securities held by third parties such as sub custodians and depositories are accurately recorded and regularly reconciled.

Safeguarding assets

- A15.** Assets held (including investments held with depositories, cash and physically held assets) are safeguarded from loss, misappropriation and unauthorised use.
- A16.** Assets held are appropriately registered and client money is segregated.

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- A17.** Appropriate segregation exists between the service organisation's custody and other operations, including asset management operations, which may give rise to a conflict of interest⁹⁵

Monitoring compliance

- A18.** Transaction errors are rectified promptly.

Monitoring Subservice Organisations⁹⁶

- A19.** Appointments of sub-service organisations, including sub-custodians, are approved, sub-service organisations are managed in accordance with the requirements of the client agreement and their activities are adequately monitored.

Reporting

- A20.** Client reporting in respect of client asset holdings is complete and accurate and provided within required timescales.
- A21.** Asset positions and details of securities lent (including collateral) are reported to interested parties accurately and within the required time scale, including those responsible for initiating voting instructions.

Information technology

G.1 – G.14

⁹⁵ Control objective applies if the custodian also provides asset management services.
⁹⁶ Control objective for monitoring subservice organisations applies when the carve-out method is used to deal with subservice organisations.

Appendix 3

B. Asset Management

Definition:

“Asset management” is the investment of money on behalf of clients and involves the performance of the following functions:

- Initiating and executing purchase and sale transactions, either by specific direction from the client or under discretionary authority granted by the client.
- Determining whether transactions comply with guidelines and restrictions.
- Reconciling records of security transactions and portfolio holdings, for each client, to statements received from the custodian.
- Reporting to the client on portfolio performance and activities.

Asset may be managed in accordance with specific client directions; under a discretionary mandate agreed by the client or through a unitised fund, with the investment strategy mandated in an offer document or client agreement. Unitised funds will usually need to include both asset management and registry minimum control objectives in order to address the services provided to clients.

Control Objectives:

Accepting clients

- B.1** Accounts are set up completely and accurately in accordance with client agreements and/or offer documents and applicable regulations.
- B.2** Complete and authorised client agreements, including investment guidelines and restrictions, are established prior to initiating investment activity.

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Authorising and processing transactions

- B.3** Asset investment transactions are properly authorised, executed and allocated in a timely and accurate manner.
- B.4** Transactions are undertaken only with approved brokers.
- B.5** Asset investment and related cash transactions are completely and accurately recorded and settled in a timely manner.
- B.6** Corporate events and proxy voting instructions are identified and generated, respectively, and then actioned, processed and recorded accurately and in a timely manner.
- B.7** Client new monies and withdrawals are processed and recorded completely and accurately, withdrawals are authorised.⁹⁷

Maintaining financial and other records

- B.8** Accounts are administered in accordance with client agreements and/or offer documents.
- B.9** Changes to non-monetary client data (for example, address changes and changes in allocation instructions) are authorised and correctly recorded on a timely basis.⁹⁸
- B.10** Investment income and related tax are accurately recorded in the proper period.
- B.11** Investments are valued using current prices obtained from independent external pricing sources or an alternative basis in

⁹⁷ For unitised funds this objective is not usually applicable as investments are made or withdrawn by the purchase or sale of units, however instead the control objectives for Registry (Section F) will need to be addressed.

⁹⁸ For unitised funds this objective is covered by the control objectives for Registry (Section F) which will also need to be addressed.

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accordance with client agreements in circumstances where independent sources are not available.⁹⁹

B.12 Cash and securities positions are completely and accurately recorded and reconciled to third party data.

B.13 Investment management fees and other account expenses are accurately calculated and recorded in accordance with client agreements and/or offer documents.

Safeguarding of assets

B.14 Investments are properly registered and client money is segregated¹⁰⁰.

B.15 Appropriate segregation exists between the service organisation's asset management and other operations, including custody services, which may give rise to a conflict of interest.¹⁰¹

Monitoring compliance

B.16 Client portfolios are managed in accordance with investment objectives, monitored for compliance with investment guidelines and restrictions and performance is measured.

B.17 Transaction errors (including investment guideline breaches) are rectified promptly and clients treated fairly.

B.18 Broker exposures are monitored in accordance with client agreements and/or offer document.

⁹⁹ This objective is not intended to extend to the detailed controls over unit pricing.

¹⁰⁰ For unitised funds this objective is amended to "investments are properly registered" as clients' funds are pooled rather than segregated

¹⁰¹ Control objective applies if the investment administrator also provides other services, including custody, which may give rise to a conflict of interest.

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Appendix 3

Monitoring Subservice Organisations¹⁰²

B.19 Appointments of sub-service organisations, including those providing asset management services, are approved, sub-service organisations are properly managed and their activities are adequately monitored on a timely basis.

Reporting to clients

B.20 Client reporting in respect of portfolio transactions and holdings (including collateral) is complete and accurate and provided within required timescales.

Information technology

G.1 – G.14

¹⁰² Control objective for monitoring subservice organisations applies when the carve-out method is used to deal with subservice organisations.

Appendix 3

C. Property Management

Definition:

“Property management” is the performance of the following functions:

- Initiating and executing property purchase and sale transactions either by specific direction from the client or under discretionary authority granted by the client.
- Determining whether transactions comply with guidelines and restrictions.
- Reconciling records of transactions for each client, to statements received from the custodian.
- Reporting to the client on performance and activities.

Control Objectives:

Accepting clients

- C.1** Accounts are set up completely and accurately in accordance with client agreements and applicable regulations.
- C.2** Complete and authorised client agreements are established prior to initiating investment activity.
- C.3** Investment guidelines and restrictions are established and agreed prior to investment management activity.
- C.4** Unitholder activity is recorded completely, accurately and in a timely manner.

Authorising and processing transactions

- C.5** Investment decisions are properly formulated in accordance with investment guidelines, authorised, implemented and reviewed on a timely basis.

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- C.6** Property developments are only undertaken in accordance with acceptable risk criteria.
- C.7** Costs associated with buying and selling properties are authorised and recorded accurately.
- C.8** Tenants' covenants and lease conditions are assessed and authorised on a timely basis.
- C.9** Property and related cash transactions are completely and accurately recorded and settled in a timely manner.
- C.10** Rental income and service charges are accurately calculated and recorded on a timely basis.
- C.11** Client new monies and withdrawals are processed and recorded completely and accurately, withdrawals are appropriately authorised.

Maintaining financial and other records

- C.12** Accounts are administered in accordance with client agreements and applicable regulations.
- C.13** Changes to non-monetary client data (for example, address changes and changes in allocation instructions) are authorised and correctly recorded on a timely basis.
- C.14** Complete and accurate records of each property are maintained.
- C.15** Properties are valued in accordance with regulatory requirements, client agreements or industry standard. Valuations are obtained at regular intervals from independent external valuers.
- C.16** Income entitlements are received in full, wherever possible, and expenses, both recoverable and irrecoverable, are controlled.
- C.17** Property management fees and other account expenses are accurately calculated and recorded.

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- C.18** Rents are monitored and rent reviews are recorded promptly and accurately.
- C.19** Unitholders' funds are priced and administered accurately and in a timely manner.

Safeguarding assets

- C.20** Properties purchased are of good and marketable title.
- C.21** Title deeds are safeguarded from loss, misappropriation and unauthorised use.
- C.22** Uninvested cash is appropriately registered and client money is segregated.
- C.23** Risks arising from investing in property are insured where this is economic to the interests of owners (for example consider claims etc. arising from the public where large shopping malls are owned).
- C.24** Appropriate segregation exists between the service organisation's property management and other operations, which may give rise to a conflict of interest.¹⁰³

Monitoring compliance

- C.25** Client portfolios are managed in accordance with investment objectives, monitored for compliance with investment guidelines and restrictions and performance is measured.
- C.26** Transaction errors (including guideline breaches) are rectified promptly.

¹⁰³ Control objective applies if the property manager also provides other services which may give rise to a conflict of interest.

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Monitoring Subservice Organisations¹⁰⁴

C.27 Appointments of sub-service organisations, including those providing property management services, are approved, sub-service organisations are properly managed and their activities are adequately monitored on a timely basis.

Reporting to clients

C.28 Client reporting in respect of property transactions, holdings and performance is complete and accurate and provided within required timescales.

Information technology

G.1 – G.14

¹⁰⁴ Control objective for monitoring subservice organisations applies when the carve -out method is used to deal with subservice organisations.

Appendix 3

D. Superannuation Member Administration

Definition:

“Superannuation member administration” is the performance of the following functions:

- Maintaining membership data, including the addition of new members and updating existing members’ data.
- Receiving contributions and transfers in from employers, members or government and allocating to members accounts.
- Calculation and payment of benefits to members, beneficiaries, other superannuation funds and/or other third parties where applicable (e.g. financial hardship).
- Receiving instructions from members and trustees regarding investment elections and investment switch requests, and communicating these instructions to other service organisations responsible for executing these instructions.
- Processing deductions from member accounts, including insurance premiums, administration fees and contribution tax, and remittance of expenses and tax to appropriate parties.
- Liaison with insurers regarding insurance claims, receipt of insurance proceeds and payment of death, TPD and income protection benefits.
- Allocation of fund earnings to members’ accounts, through application of crediting rate or adjustment of unit prices.
- Annual review of fund, including roll up of members’ accounts and calculation of vested benefits/accrued benefits and annual reporting to members and trustees.

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Where the service organisation maintains financial records in addition to member records, the control objectives in Appendix 3 Section E Investment Administration will be applicable.

Control Objectives:

Accepting clients

- D.1** Accounts for superannuation funds and sub-plans are set up completely and accurately in accordance with client agreements and applicable regulations.
- D.2** Member accounts are set up completely and accurately in accordance with fund rules and individual investment and insurance elections.

Authorising and processing transactions

- D.3** Contributions and transfers in are correctly classified and allocated to members' accounts, processed accurately and on a timely basis.
- D.4** Superannuation benefits payable and transfer values are calculated and recorded accurately and payments are authorised and made on a timely basis.
- D.5** Instructions from members and trustees regarding investment elections and investment switch requests are actioned and accurately processed.
- D.6** Deductions from member accounts, including insurance premiums, administration fees and contribution tax, are calculated in accordance with member elections, fund rules, relevant legislation and regulations and accurately recorded.
- D.7** Expenses and tax deducted are remitted to the appropriate parties on a timely basis.

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Maintaining member records

- D.8** Changes to members' standing data (for example, address changes and changes in allocation instructions) are authorised and correctly recorded on a timely basis.
- D.9** Investment earnings are accurately allocated (through crediting rates or unit pricing) to member accounts and in accordance with trustee directions and fund rules.

Safeguarding assets

- D.10** Superannuation fund, sub-plan and member data is appropriately stored to ensure security and protection from unauthorised use
- D.11** Appropriate segregation exists between the service organisation's superannuation member administration and other operations, which may give rise to a conflict of interest.¹⁰⁵

Monitoring compliance

- D.12** Contributions are received in accordance with fund rules and relevant legislation.
- D.13** Transaction errors are identified, notified to members or trustees in accordance with client agreements and rectified promptly if required.
- D.14** Benefits payable and transfer values are calculated and paid in accordance with superannuation fund rules, relevant legislation and regulations.

¹⁰⁵ Control objective applies if the property manager also provides other services which may give rise to a conflict of interest.

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Monitoring Subservice Organisations¹⁰⁶

D.15 Appointments of sub-service organisations, including those providing superannuation member administration, are approved, sub-service organisations are properly managed [CG7] and their activities are adequately monitored on a timely basis.

Reporting to clients

D.16 Annual member statements issued to members are accurate and complete and distributed on a timely basis.

Information technology

G.1 – G.14

¹⁰⁶ Include control objectives for monitoring subservice organisations when the carve -out method is used to deal with subservice organisations.

Appendix 3

E: Investment Administration

Definition:

“Investment Administration” is the performance of the following functions:

- Maintaining records of securities, cash, and other portfolio assets and liabilities based on information received from the Trustee/Responsible Entity, investment manager, registrar, custodian and others (as applicable).
- Valuations of portfolio assets and liabilities, determining net asset values and reporting thereof.
- Periodic reporting of performance and investment compliance to the Trustee/Responsible Entity, investment manager, and others (as applicable).
- Periodic financial reporting.

Unit pricing and crediting rate calculations are also a function performed in investment administration, for which the control objectives include the accurate calculation of daily or other periodic unit prices or crediting rates with detailed controls allied to that objective. Control objectives relevant to unit pricing, distributions and credit rate calculations have not been listed below, because it would not ordinarily be necessary to meet these objectives in obtaining assurance over the operating effectiveness of controls for investment administration services provided by a service organisation for the purpose of the audit of user entities’ financial reports.

Control Objectives:

Accepting clients

- E.1** Accounts are set up completely and accurately in accordance with client agreements and applicable regulations.
- E.2** Complete and authorised client agreements are established prior to initiating accounting activity.

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Authorising and processing transactions

- E.3** Portfolio transactions are recorded completely, accurately and on a timely basis.
- E.4** Corporate actions are actioned, processed and recorded accurately and on a timely basis.
- E.5** Expenses are appropriately authorised and recorded in accordance with the service level agreement and/or client instructions, on a timely basis.
- E.6** Appropriate segregation exists between the service organisation's investment administration and other operations, which may give rise to a conflict of interest.¹⁰⁷[AC8]

Maintaining financial and other records

- E.7** Accounts are administered in accordance with client agreements.
- E.8** Changes to non-monetary static data (for example, address changes and changes in allocation instructions) are authorised and correctly recorded on a timely basis.
- E.9** Investment income and related tax are accurately calculated and recorded on a timely basis.
- E.10** Investments are valued using current prices obtained from independent external pricing sources, or an alternative basis in accordance with client agreements in circumstances where independent sources are not available.
- E.11** Issue and cancellations of shares/units are recorded completely and accurately in the financial records and units on issue are regularly reconciled to data provided by registry. Cash and securities

¹⁰⁷ Control objective applies if the property manager also provides other services which may give rise to a conflict of interest.

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positions are completely and accurately recorded and reconciled to third party data on a timely basis.

- E.12** Reconciliations between different systems, including the investment ledger, general ledger and administration system, are performed on a timely basis.

Monitoring compliance

- E.13** Errors are identified, notified to clients and rectified promptly in accordance with client agreements

Monitoring Subservice Organisations¹⁰⁸

- E.14** Appointments of sub-service organisations, including those providing investment administration, are approved, sub-service organisations are properly managed and their activities are adequately monitored on a timely basis.

Reporting to clients

- E.15** Periodic reports to clients, including calculation of net asset value if required, are accurate and complete and distributed on a timely basis.

- E.16** Annual reports and accounts are prepared in accordance with applicable laws and regulations.

Taxation

- E.17** Tax Policy is updated and reviewed on a timely basis.

- E.18** Tax information components and attributes used in the preparation of the income tax computation (current and deferred) are complete and calculated accurately in accordance with tax policy or as agreed with clients.

¹⁰⁸ Include control objectives for monitoring subservice organisations when the carve -out method is used to deal with subservice organisations.

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E.19 **[CG9]** Differences between tax and accounting treatments are identified and calculated in accordance with tax policy or as agreed with clients and reported in a timely manner to clients.

E.20 Current and deferred tax balances in the general ledger are accurately recorded in accordance with the tax computation, and processed in a timely manner in accordance with tax policy or as agreed with clients.

[CG10] Information technology

G.1 – G.14

Draft

Appendix 3

F. Registry

Definition:

“Registry” is the performance of the following functions:

- Maintaining records of the name and address of each shareholder or unitholder investing in the client/issuer, the amount of shares or units in the client owned by each share/unitholder, any reference corresponding to a share/unit holder’s positions, the issue date of the share/unit, and the cancellation date of the share/unit (if applicable).
- Recording the amount of shares/units purchased, redeemed, switched, transferred or reinvested by a shareholder or unitholder on the issuer’s books upon receipt of a validated request.
- Recording changes to share/unit holdings as a consequence of a corporate action upon receipt of a validated instruction.
- Monitoring the issuance of shares/units in an issue to prevent the unauthorised issuance of shares/units.
- Ensuring that any issuance of shares/units will not cause the authorised number of shares/units in an issue to be exceeded and that the number of new shares/units represented corresponds to the number of cancelled shares/units.
- Performing stakeholder meeting and voting processes such as document design and print procurement, postage, other distribution of documentation and reporting.

Service organisations providing unitised products will usually need to address both the asset management and registry control objectives, as these products include both services for clients.

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Control Objectives:

Accepting clients

- F.1** Accounts are set up completely and accurately in accordance with client/issuers agreements.
- F.2** Complete and authorised client agreements are established prior to initiating accounting activity.

Authorising and processing transactions

- F.3** New share/unitholder activity is clearly established and recorded completely, accurately and in a timely manner.
- F.4** Share/unitholder applications, redemptions and switches received are checked, sorted and distributed for processing in a timely manner.
- F.5** Share/unitholder transactions and adjustments are authorised, processed accurately, completely and in a timely manner.
- F.6** Cash receipts are processed accurately and banked promptly.
- F.7** Cheques and confirmation letters issued are accurately generated, matched and authorised prior to despatch.
- F.8** Where issued capital is fixed, the number of shares in the registry records match the number of shares on issue..
- F.9** Distribution payments and reinvestments are complete, calculated in accordance with the authorised distribution and processed in a timely manner.

Maintaining financial and other records

- F.10** Accounts are administered in accordance with client agreements.

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- F.11** Changes to non-monetary share/unitholder data (for example, address changes and changes in allocation instructions) are authorised and correctly recorded on a timely basis.
- F.12** Registrar records accurately reflect shares, units and cash held by third parties.
- F.13** Share/unit activity is recorded completely, accurately and positions are regularly reconciled.¹⁰⁹[CG11]

Safeguarding assets

- F.14** Lost and stolen certificates are recorded in a timely manner.
- F.15** Appropriate segregation exists between the service organisation's registry services and other operations, which may give rise to a conflict of interest.¹⁰⁹[AC12]

Monitoring compliance

- F.16** Transaction errors are identified, notified to clients and share/unit holders in accordance with client agreements and rectified if necessary.

Monitoring Subservice Organisations¹¹⁰

- F.17** Appointments of sub-service organisations, including those providing registry services, are approved, sub-service organisations are properly managed and their activities are adequately monitored on a timely basis.

Reporting to clients

- F.18** Client reporting is complete and accurate and processed within required timescales.

¹⁰⁹ Control objective applies if the registry also provides other services which may give rise to a conflict of interest.

¹¹⁰ Include control objectives for monitoring subservice organisations when the carve -out method is used to deal with subservice organisations.

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Taxation

F.19 Withholding tax for non-residents, or where no TFN/ABN has been provided, is calculated completely, accurately and on a timely basis.

Information technology

G.1 – G.14

Draft

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G. Information Technology

Scope:

Information technology (IT) control objectives are applicable to all investment management services as IT is integral to providing those services. The IT control objectives are addressed for each investment management service reported on, in addition to the specific control objectives that are provided for each investment management service in this Appendix. The IT systems which are addressed in the controls identified to meet these objectives are those which are relevant to the investment management services provided to user entities, specifically the financial reporting of user entities with respect to those services.

Control Objectives:

Restricting access to systems and data

- G.1** [CG13] Physical access to computer networks, equipment, storage media and program documentation is restricted to authorised individuals.
- G.2** Logical access to computer systems, programs, master data, client data, transaction data and parameters, including access by administrators to applications, databases, systems and networks, is restricted to authorised individuals via information security tools and techniques.
- G.3** Segregation of incompatible duties is defined, implemented and enforced by logical security controls in accordance with job roles.

Authorising and processing transactions

- G.4** IT processing is authorised and scheduled appropriately and exceptions are identified and resolved in a timely manner.

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Safeguarding assets

- G.5** Appropriate measures, including firewalls and anti-virus software, are implemented to counter the threat from malicious electronic attack.
- G.6** The physical IT equipment is maintained in a controlled environment.
- G.7** Appropriate segregation exists between the service organisation's IT and other operations, which may give rise to a conflict of interest.¹¹¹

Maintaining and developing systems hardware and software

- G.8** Development and implementation of new systems, applications and software, and changes to existing systems, applications and software, are authorised, tested, approved, implemented and documented.
- G.9** Data migration or modification is authorised, tested and, once performed, reconciled back to the source data.

Recovering from processing interruptions

- G.10** Data and systems are backed up regularly offsite and tested for recoverability on an annual basis.
- G.11** IT hardware and software issues are monitored and resolved in a timely manner.
- G.12** Business and information systems recovery plans are documented, approved, tested and maintained.

¹¹¹ Control objective applies if the IT manager also provides other services which may give rise to a conflict of interest.

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Monitoring compliance

- G.13** Information technology services provided to clients are approved, managed and performance thresholds met in accordance with the requirements of the client agreement.

Monitoring Subservice Organisations¹¹²

- G.14** Appointment of sub-service organisations, including those providing IT services, are approved, sub-service organisations are managed in accordance with the requirements of the client agreement and their activities are adequately monitored.

¹¹² Include control objectives for monitoring subservice organisations when the carve -out method is used to deal with subservice organisations.

Appendix 4

(Ref: para. 65)

SERVICE AUDITOR'S TYPE 2 ASSURANCE REPORT

Independent Service Auditor's Assurance Report on the Description of Controls over [Investment Management Service], their Design and Operating Effectiveness

To: XYZ Service Organisation

Scope

We have been engaged to report on XYZ Service Organisation's (XYZ) description at pages [bb-cc] of its [specify investment management service: custody, asset management, property management, superannuation member administration, investment administration or registry] system provided to XYZ's clients throughout the period [date] to [date] (the description), and on the design and operations of those controls related to the control objectives stated in the description.¹¹³

XYZ's Responsibilities

XYZ is responsible for: preparing the description and accompanying assertion at page [aa], including the completeness, accuracy and method of presentation of the description and assertion; providing the [investment management service] services covered by the description; stating the control objectives, including the minimum controls objectives for [investment management service/s] from *Guidance Statement GS 007 Audit Implications of the Use of Service Organisations for Investment Management Services*; providing and explanation for any omissions or modifications to the minimum control objectives and designing, implementing and effectively operating controls to achieve the stated control objectives.

¹¹³ If some elements of the description are not included in the scope of the engagement, this is made clear in the assurance report.

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Service Auditor's Responsibilities

Our responsibility is to express an opinion on XYZ's description and on the design and operation of controls related to the control objectives stated in that description based on our procedures. We conducted our engagement in accordance with Standard on Assurance Engagements ASAE 3402 *Assurance Reports on Controls at a Service Organisation*, issued by the Auditing and Assurance Standards Board. That standard requires that we comply with relevant ethical requirements and plan and perform our procedures to obtain reasonable assurance about whether, in all material respects, the description is fairly presented and the controls are suitably designed and operating effectively.

An assurance engagement to report on the description, design and operating effectiveness of controls at a service organisation involves performing procedures to obtain evidence about the disclosures in the service organisation's description of its system, and the design and operating effectiveness of controls. The procedures selected depend on our judgement, including the assessment of the risks that the description is not fairly presented, and that controls are not suitably designed or operating effectively. Our procedures included testing the operating effectiveness of those controls that we consider necessary to provide reasonable assurance that the control objectives stated in the description were achieved. An assurance engagement of this type also includes evaluating the overall presentation of the description, the suitability of the objectives stated therein, and the suitability of the criteria specified by the service organisation and described at page [aa].

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

Limitations of Controls at a Service Organisation

XYZ's description is prepared to meet the common needs of a broad range of clients and their auditors and may not, therefore, include every aspect of the system that each individual client may consider important in its own particular environment. Also, because of their nature, controls at a service organisation may not prevent or detect all errors or omissions in processing or reporting transactions. Also, the projection of any evaluation of

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effectiveness to future periods is subject to the risk that controls at a service organisation may become inadequate or fail.

Opinion

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

- (a) The description fairly presents the [investment management service] system as designed and implemented throughout the period from [date] to [date];
- (b) The controls related to the control objectives stated in the description were suitably designed throughout the period from [date] to [date]; and
- (c) The controls tested, which were those necessary to provide reasonable assurance that the control objectives stated in the description were achieved, operated effectively throughout the period from [date] to [date].

Description of Tests of Controls

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

Intended Users and Purpose

This report and the description of tests of controls on pages [yy-zz] are intended only for clients who have used XYZ's [investment management service] system, and their auditors, who have a sufficient understanding to consider it, along with other information including information about controls operated by clients themselves, when assessing the risks of material misstatements of clients' financial reports/statements.

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Appendix 4

[*Service Auditor's signature*]

[*Date of the service auditor's assurance report*]

[*Service auditor's address*]

Draft

Appendix 5

(Ref: Para. 66)

SERVICE AUDITOR'S DESCRIPTION OF THE NATURE, TIMING AND EXTENT OF TESTS APPLIED TO CONTROLS

The description does not duplicate the service auditor's detailed assurance programme, since that would provide more than the appropriate level of detail. There is no standardised format for presenting a description of tests applied to controls, however the following elements are ordinarily included in the description:

1. Cross reference to the control objectives and allied controls¹¹⁴ intended to achieve those objectives described in the service organisation's description of its system.
2. Assessment of the fair presentation of the description, including:
 - (a) identification of any inadequacies, omissions or inaccuracies in the description of control objectives;
 - (b) identification of any inaccuracies in the description of controls, as designed and implemented.
3. Assessment of the suitability of the design, including identification of any inadequacies in the design of the controls to achieve their stated objectives.
4. Tests of operating effectiveness, including:
 - (a) nature, timing and extent of tests conducted including whether the whole population was tested or a sample, in this case the size of the sample;
 - (b) number and nature of exceptions noted;

¹¹⁴ If applicable, complementary user entity controls would also be described.

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- (c) remedial action taken by management, if any; and
- (d) results of the tests in sufficient detail to enable user auditors to assess the effect of those tests on their assessment of control risk.

Description of nature of tests

The nature of tests carried out by the service auditor may include such procedures as enquiry, inspection, observation and re-performance. Examples of descriptions of these procedures, which may assist the service auditor in describing tests of controls are set out below.

1. Enquiry:
 - Enquired of appropriate XYZ personnel.
 - Conducted enquiries seeking relevant information or representation from personnel were performed to obtain, among other things:
 - Knowledge, additional information and affirmation regarding the control of procedures.
 - Corroborating evidence of the controls.
2. Inspection:
 - Inspected documents and records indicating performance of the controls. This included, among other things:
 - Inspection of reconciliations and management reports that age and/or quantify reconciling items to assess whether balances and reconciling items appear to be properly monitored, controlled and resolved on a timely basis, as required by the related control.

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- Examination of source documentation and authorisations related to selected transactions processed.
 - Examination of documents or records for evidence of performance, such as the existence of initials or signatures.
 - Inspection of XYZ's systems documentation, such as operations, manuals, flow charts and job descriptions.
3. Observation:
- Observed the application or existence of specific controls as represented.
4. Re-performance:
- Re-performed the control or processing application of the controls to check the accuracy of their operation. This included, among other things:
 - Obtaining evidence of the arithmetical accuracy and correct processing of transactions by performing independent calculations.
 - Re-performing the matching of various system records by independently matching the same records and comparing reconciling items to reconciliations prepared by XYZ.

Appendix 6

(Ref: Para. 82)

ILLUSTRATIONS OF SERVICE AUDITOR'S REPORTS ON FINANCIAL INFORMATION

The following example Service Auditor's Reports are for use as a guide only, in conjunction with the considerations described in GS 007, and will need to be varied according to individual requirements and circumstances.

Example 1: Service Auditor's Report on Specified Assertions

Independent Auditor's Report

To [those charged with governance] of XYZ Service Organisation (XYZ) regarding [user entity]

Report on Specified Assertions of Assets [and liabilities or transactions] in the Statement¹¹⁵

We have audited the [specify assertions audited: for transactions or events: occurrence, completeness, accuracy, cut-off and classification; for balances: existence, rights and obligations, completeness or valuation and allocation; or for presentation and disclosure: occurrence, rights and obligations, completeness, classification and understandability and accuracy and valuation] of the assets [and liabilities or transactions] of the accompanying [title of financial statement] ("the Statement"), which comprises the [statement of assets and liabilities] as at [date], and the [statement of transactions] for the year then ended, concerning the assets [and liabilities or transactions] of [user entity]¹¹⁶ for which XYZ provides [specify investment management service provided: custody, asset management, property management, superannuation member administration, investment

¹¹⁵ The subheading "Report on the Statement" is unnecessary in circumstances when the second subheading "Report on Other Legal and Regulatory Requirements" is not applicable.

¹¹⁶ Where the assets are held in the name of a nominee holding company insert "held in the name of [nominee holding company]".

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administration or registry] services, set out on pages [] to []¹¹⁷. The Statement has been prepared on the basis on accounting described in note X.

Management’s Responsibility for the Statement

XYZ is responsible for [investment management service] on behalf of [user entity]. Management is responsible for the preparation and fair presentation of the Statement in accordance with [specify framework applied]¹¹⁸ and have determined that the accounting policies described in Note X to the Statement are appropriate to meet the financial reporting requirements of the [title of contract or service level agreement] and are appropriate to meet the needs of [user entity]. Management are also responsible for such internal control as management determines is necessary to enable the preparation of the Statement that is free from material misstatement, whether due to fraud or error.

Auditor’s Responsibility

Our responsibility is to express an opinion on the [specify assertions audited] in respect of the assets [and liabilities or transactions] in the accompanying Statement, based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those Standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the assets [and liabilities or transactions] set out in the Statement are free of material misstatement in respect of the specified audit assertions.

An audit of [specify assertions audited] of the assets [and liabilities or transactions] in the Statement involves performing procedures to obtain audit evidence that the assets [and liabilities or transactions] set out in the Statement [insert relevant assertion: for example for existence insert “exist as

¹¹⁷ When the auditor is aware that the Statement will be included in a document that contains other information, the auditor may consider, if the form of the presentation allows, identifying the page numbers on which the Statement is presented.

¹¹⁸ Insert “applicable Australian Accounting Standards” where multiple Australian Accounting Standards were applied; insert reference to specific Australian Accounting Standard where appropriate (for example: “in accordance with the measurement standards of AAS 25 *Financial Reporting by Superannuation Plans*.”); or “the accounting policies described in Note X to the Statement”.

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at [date]” or for valuation insert: “have been appropriately valued in accordance with [specify framework]”¹¹⁹. The procedures selected depend on the auditor’s judgement, including the assessment of the risks of material misstatement of the Statement in relation to the specified assertions, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to XYZ’s preparation and fair presentation of the Statement 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 XYZ’s controls¹²⁰. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, if any, made by management with respect to the specified assertions.

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

[Insert either: No uncorrected misstatements, other than amounts which are clearly trivial, have been identified during the course of our audit; Or: uncorrected misstatements, other than amounts which are clearly trivial, which, have come to our attention during the course of our audit and are not material individually or in aggregate in relation to the [specify assertions audited] in respect of the assets [and liabilities or transactions] in the accompanying Statement but may be material when aggregated with any uncorrected misstatements identified by [user entity]’s Auditor, are listed in an attachment to this report. These uncorrected misstatements do not affect our audit opinion.]

¹¹⁹ Insert “applicable Australian Accounting Standards” where multiple Australian Accounting Standards were applied; insert reference to specific Australian Accounting Standard where appropriate (for example: “in accordance with the measurement standards of AAS 25 *Financial Reporting by Superannuation Plans*.”) or “the accounting policies described in Note X to the Statement”.

¹²⁰ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the Statement, this sentence would be worded as follows: “In making those risk assessments, the auditor considers internal control relevant to XYZ’s preparation and fair presentation of the Statement in order to design audit procedures that are appropriate in the circumstances.”

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Opinion

In our opinion, the Statement presents fairly, in all material respects, the [specify assertions audited] of the assets [and liabilities or transactions] of [user entity], for which XYZ provides [investment management service] services, as of [date] in accordance with [specify framework].¹²¹

Basis of Accounting and Restriction on Distribution

Without modifying our opinion, we draw attention to Note X to the Statement, which describes the basis of accounting. The Statement has been prepared by XYZ for distribution to the [the Trustee/those charged with governance] of [user entity]. Our report is intended solely for XYZ, [user entity] and their auditor and should not be distributed to any other parties or used for any other purpose other than that for which they are prepared.¹²²

Report on Other Legal and Regulatory Requirements

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities].

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

¹²¹ Insert "applicable Australian Accounting Standards" where multiple Australian Accounting Standards were applied; insert reference to a specific Australian Accounting Standard where appropriate (for example: "the measurement standards of AAS 25 Financial Reporting by Superannuation Plans."; or "the accounting policies described in note X to the Statement").

¹²² Use of the report & liability limitation: insert additional/alternative wording, if any, required to reflect any liability arrangements agreed between the service auditor, the service organisation and other users, including confirmation of the purpose for which the service auditor's report has been prepared and the basis on which other parties may use the report.

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[Attachment: Uncorrected Misstatements]¹²³

In the course of conducting our audit procedures at XYZ for the purpose of reporting on [specific assertions] we have identified the following uncorrected misstatements, other than amounts which are clearly trivial, which were determined by [management/those charged with governance] to be immaterial, both individually and in aggregate, to the [specific assets and liabilities or transactions] taken as a whole. These misstatements are reported solely for the purpose of providing information to clients of XYZ and their auditors and they do not affect our audit opinion:

[Insert: List of uncorrected misstatements]

¹²³ Include attachment where uncorrected misstatements were identified.

Appendix 6

Example 2: Service Auditor’s Report on a Statement

Independent Auditor’s Report

To [those charged with governance] of XYZ Service Organisation (XYZ) regarding [user entity].

Report on the Statement¹²⁴

We have audited the accompanying [title of financial statement] ("the Statement"),¹²⁵ which comprises of the [statement of assets and liabilities] as at [date], and the [statement of transactions] for the year then ended, concerning the assets [and liabilities or transactions] of [user entity]¹²⁶ for which XYZ provides [specify investment management services provided: custody, asset management, property management, superannuation member administration, investment administration or registry] services set out on pages [] to [].¹²⁷ The Statement has been prepared on the basis of accounting described in note X.

Management’s¹²⁸ Responsibility for the Statement

XYZ is responsible for [investment management service] on behalf of [user entity]. Management is responsible for the preparation and fair presentation of the Statement in accordance with [specify framework]¹²⁹ and have determined that the accounting policies described in Note X to the Statement

¹²⁴ The subheading “Report on the Statement” is unnecessary in circumstances when the second subheading “Report on Other Legal and Regulatory Requirements” is not applicable.

¹²⁵ If certain assertions are specifically excluded from the audit then insert: “except for [specify assertions excluded, e.g. presentation & disclosure] of the statement.”

¹²⁶ Where the assets are held in the name of a nominee holding company insert “held in the name of [nominee holding company].”

¹²⁷ When the auditor is aware that the Statement will be included in a document that contains other information, the auditor may consider, if the form of the presentation allows, identifying the page numbers on which the Statement is presented.

¹²⁸ Insert the title of those charged with governance – e.g. directors/trustees/committees. For example, “Director’s Responsibility for the Statement”. Insert appropriate title, when prompted, throughout the report.

¹²⁹ Insert “applicable Australian Accounting Standards” where multiple Australian Accounting Standards were applied; insert reference to specific Australian Accounting Standard where appropriate (for example: “in accordance with the measurement standards of AAS 25 *Financial Reporting by Superannuation Plans*.”) or “the accounting policies described in Note X to the Statement”.

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Appendix 6, Example 2

are appropriate to meet the financial reporting requirements of the [title of contract or service level agreement] and are appropriate to meet the needs of [user entity]. Management are also responsible for such internal control as management determines is necessary to enable the preparation of the Statement that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the Statement based on our audit. No opinion is expressed as to whether the accounting policies used, as described in Note X, are appropriate to meet the needs of [user entity]. We conducted our audit in accordance with Australian Auditing Standards. Those Standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the Statement is free from material misstatement.

An audit of the Statement involves performing procedures to obtain audit evidence about the amounts and disclosures in the Statement. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the Statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to XYZ's preparation and fair presentation of the Statement 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 XYZ's controls¹³⁰. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, if any, made by management, as well as evaluating the overall presentation of the Statement.

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

¹³⁰ In circumstances when the auditor also has responsibility to express an opinion on the effectiveness of internal control in conjunction with the audit of the Statement, this sentence would be worded as follows: "In making those risk assessments, the auditor considers internal control relevant to XYZ's preparation and fair presentation of the Statement in order to design audit procedures that are appropriate in the circumstances."

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Appendix 6, Example 2

[Insert either: No uncorrected misstatements, other than amounts which are clearly trivial, have been identified during the course of our audit; Or: uncorrected misstatements, other than amounts which are clearly trivial, which, have come to our attention during the course of our audit and are not material individually or in aggregate in relation to the Statement but may be material when aggregated with any uncorrected misstatements identified by [user entity]'s Auditor, are listed in an attachment to this report. These uncorrected misstatements do not affect our audit opinion.]

Opinion

In our opinion, the attached Statement presents fairly, in all material respects, the assets [and liabilities] of [user entity] as of [date] and transactions for the [period] then ended, for which XYZ provides [investment management service] services, in accordance with in accordance with the basis of accounting described in Note X.¹³¹

Basis of Accounting and Restriction on Distribution

Without modifying our opinion, we draw attention to Note X to the Statement, which describes the basis of accounting. The Statement has been prepared by XYZ for distribution to the [the Trustee/those charged with governance] of [user entity]. As a result, the schedule may not be suitable for another purpose. Our report is intended solely for XYZ, [user entity] and their auditor and should not be distributed to any other parties or used for any other purpose other than that for which they are prepared.¹³²

¹³¹ Insert “applicable Australian Accounting Standards” where multiple Australian Accounting Standards were applied; insert reference to a specific Australian Accounting Standard where appropriate (for example: “the measurement standards of AAS 25 Financial Reporting by Superannuation Plans.”); or “the accounting policies described in Note X to the Statement”.

¹³² Use of the report & liability limitation: insert additional/alternative wording, if any, required to reflect any liability arrangements agreed between the service auditor, the service organisation and other users, including confirmation of the purpose for which the service auditor’s report has been prepared and the basis on which other parties may use the report.

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Appendix 6, Example 2

Report on Other Legal and Regulatory Requirements

[Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities].

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

[Attachment: Uncorrected Misstatements]¹³³

In the course of conducting our audit procedures at XYZ Service Organisation for the purpose of reporting on [the Statement] we have identified the following uncorrected misstatements, other than amounts which are clearly trivial, which were determined by [management/those charged with governance] to be immaterial, both individually and in aggregate, to the [specific assets and liabilities or transactions/Statement] taken as a whole. These misstatements are reported solely for the purpose of providing information to clients of XYZ and their auditors and they do not affect our audit opinion:

[Insert: List of uncorrected misstatements]

¹³³ Include attachment where uncorrected misstatements were identified.