



AUDIT &
ASSURANCE
FACULTY

re:Assurance

Perspectives on assurance

ENGAGING
BUSINESS



re:Assurance

An initiative from [the ICAEW Audit and Assurance Faculty](#)

All types of business, public and voluntary bodies, investors, governments, tax authorities, market regulators and their stakeholders need to be able to rely on credible information flows to make decisions. Confidence suffers when there is uncertainty about the integrity of information or its fitness for purpose.

The Institute of Chartered Accountants in England and Wales' (ICAEW) Audit and Assurance Faculty is a leading authority on external audit and other assurance services. It is recognised internationally by members, professional bodies and others as a source of expertise on issues related to audit and assurance.

Through the *re:Assurance* initiative, the ICAEW Audit and Assurance Faculty is promoting dialogue about external assurance: finding out where new assurance services could strengthen markets and enhance confidence by making information flows more credible; asking how the *International Framework for Assurance Engagements* can be applied and developed; and answering demands for practical guidance to meet emerging business needs.

Perspectives on assurance is a series of discussion papers within the *re:Assurance* initiative aimed at specific audiences; those with an interest in public policy, people in business and assurance practitioners. The aim of these papers is to stimulate dialogue.

Perspectives on assurance: Engaging policy makers explains the role of external assurance in society and considers public interest issues related to the provision and performance of assurance services.

Perspectives on assurance: Engaging business helps business and their stakeholders to understand the nature of external assurance, to identify business needs and expectations that could be met by external assurance and to solicit feedback based on practical experience.

Perspectives on assurance: Engaging practitioners aims to increase awareness amongst practitioners of the nature of external assurance and helps them to respond to opportunities for external assurance. It explains the key elements of the *International Framework for Assurance Engagements*, seeks feedback based on practical experience and identifies areas where there may be a need for new guidance.

Further information on the *re:Assurance* initiative, the current work programme and how to get involved is available at www.icaew.com/assurance or telephone Jo Iwasaki on + 44 (0)20 7920 8786.

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December 2007

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ISBN: 978-1-84152-531-0

Perspectives on assurance

Engaging business

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Share your views

This paper is written primarily for business and their stakeholders. The Institute of Chartered Accountants in England and Wales' (ICAEW) Audit and Assurance Faculty is committed to increasing awareness amongst business and their stakeholders of the nature of external assurance and to identify business needs and expectations.

We want to discuss the issues identified in this discussion paper with businesses and their stakeholders. Comments can be emailed to us but if you would like to talk to us please call the number below or send your contact details to our email address. Comments are requested by 30 June 2008.

In the discussion paper we pose a series of questions, which are reproduced below. We are particularly interested in views on these questions.

The discussion paper also explores a number of issues which might benefit from further research. We are keen to hear about any research which is being or could be conducted in these areas.

Opportunities for external assurance

1. This paper explains the different ways that business and their stakeholders can build trust in the credibility of information. Which of these potential solutions do you use and why?

What is external assurance?

2. External assurance may be described as the provision of an independent opinion provided by an expert practitioner on information prepared by business for the benefit of stakeholders. On what types of information do you seek external assurance and why?
3. Can you provide examples of circumstances where external assurance has helped to reinforce trust?
4. Are there types of information on which you would like external assurance that is not currently available?

Practical issues

5. The paper indicates that there are a number of different practitioners who provide external assurance reports. Who provides the external assurance reports you use and how do you satisfy yourself about the quality of these reports?
6. The paper highlights that there are a number of different external assurance reports being provided. What types of conclusions are included in external assurance reports you commission or use and are they meeting your needs?
7. Have you experienced difficulties in trying to compare external assurance reports and if so, how have you addressed these concerns?

Frameworks for external assurance services

8. For specific types of external assurance report, do you know whether the practitioner has followed a particular framework? If so, what was the framework and was it helpful to know that it had been applied?

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1. Introduction

1.1 Background

Businesses¹ continually seek opportunities to develop business relationships, to enter new markets and to adopt new practices and technologies. They may, for example, enter into new partnerships or outsource operations to third parties. Credible information flows are essential for effective business relationships but how can you know if new partners are providing trustworthy information and whether the outsourced operations are being properly monitored?

Business and their stakeholders need to rely on credible information to make effective economic decisions and for business relationships to work effectively. For information to be credible, it needs to be objective, of good quality and fit for purpose. Trust and integrity are important factors that underpin credible information flows. It is however, difficult to build trust in a complex and dynamic business world where there are new technology and business practices, changing expectations of stakeholders and demands for further information and a stream of new regulations which require increasing levels of expertise and experience.

Business and their stakeholders need suitable solutions to help address these issues and meet their information needs. One of these solutions might be external assurance.

The statutory audit of financial statements is an example of external assurance. There are, however, other areas where external assurance services are being or could be provided, for example, on information relating to internal controls, outsourced operations and compliance with contractual agreements.

1.2 The objectives and scope of this discussion paper

This discussion paper seeks to increase awareness amongst business and their stakeholders of the nature of external assurance, to identify business needs and expectations, areas where there may be a need for external assurance, to prompt feedback based on experience and to discuss practical issues. It is aimed at businesses, as preparers of information, and their stakeholders, the intended users of information.

This is one of the discussion papers in the *Perspectives on assurance* series, part of the ICAEW Audit and Assurance Faculty's *re:Assurance* initiative which promotes dialogue on assurance with interested parties. The benefits gained by business from external assurance are dependent on the ability of practitioners to deliver them and are also influenced by policy makers and the role of external assurance in society. These issues are explored separately in the other discussion papers in the series.

Over the last two decades there have been other initiatives in the area of external assurance, some of which have focused on the identification and promotion of new assurance services.² The objective of these papers, however, is to seek to engage with those who have an interest in reliable business information and, through discussion of the issues around the role of external assurance, to try to gain a broader understanding of the needs of business, their stakeholders and society at large.

¹ The term 'businesses' is used in the broadest sense of the word to encompass activities carried out by both commercial and non-commercial entities and organisations.

² For example, work carried out through the American Institute of Certified Public Accountants' (AICPA) Vision Project and Special Committee on Assurance Services, see www.cpavision.org.

2. Meeting business needs

2.1 The need for credible information flows

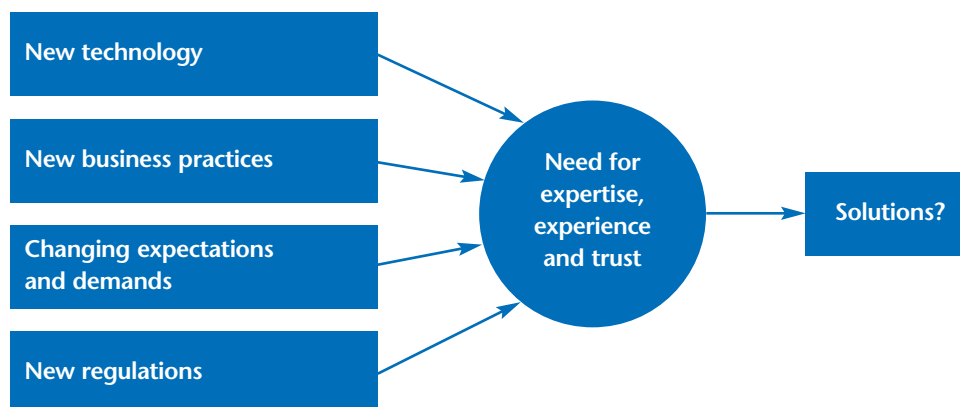
Information is central to market activities; business and their stakeholders need reliable information to make sound economic decisions. Stakeholders, such as public and voluntary bodies, investors, governments, tax authorities, market regulators, policy makers, non-governmental organisations (NGOs) and other interest groups need to have confidence in the quality of information presented to them and trust in the business that is reporting it.

Trust and integrity are important factors that underpin credible information flows and key characteristics of effective business relationships. Confidence and trust, however, diminish if there is uncertainty about the reliability of information or its fitness for purpose.

There are a number of factors that might affect the reliability and usefulness of information. The business world is constantly changing and complex. If you are in business, new technology and business practices, changing expectations of stakeholders and demands for further information and a stream of new regulations may seem quite overwhelming. You need to build and maintain trust in your business by responding to these changes but this can be difficult with the growing technical complexity of new requirements. Similarly, globalisation and changing expectations in the market place lead to new opportunities to work with different people and whilst these opportunities can help the business to grow, they require particular expertise and experience. You may question whether you have the relevant expertise and experience to deal with all of these changes and to take advantage of new opportunities in unfamiliar areas.

Business and their stakeholders need to find suitable solutions to help them address their concerns in the face of uncertainty as highlighted in figure 2.1.

FIGURE 2.1: CHALLENGES TO CREDIBILITY



2.2 Ways of building confidence

There are a number of ways that business and their stakeholders can build trust in the credibility of information and the reputation of businesses. The internal controls and internal audit functions of businesses support credible information flows and some businesses may choose to outsource specific parts of their operations to organisations with the relevant experience and expertise that is required. Likewise, businesses might engage directly with their stakeholders, through website tools, stakeholder forums and open days or other mechanisms to help ensure that stakeholders' needs are being met. This also allows for stakeholders to provide important feedback to businesses.

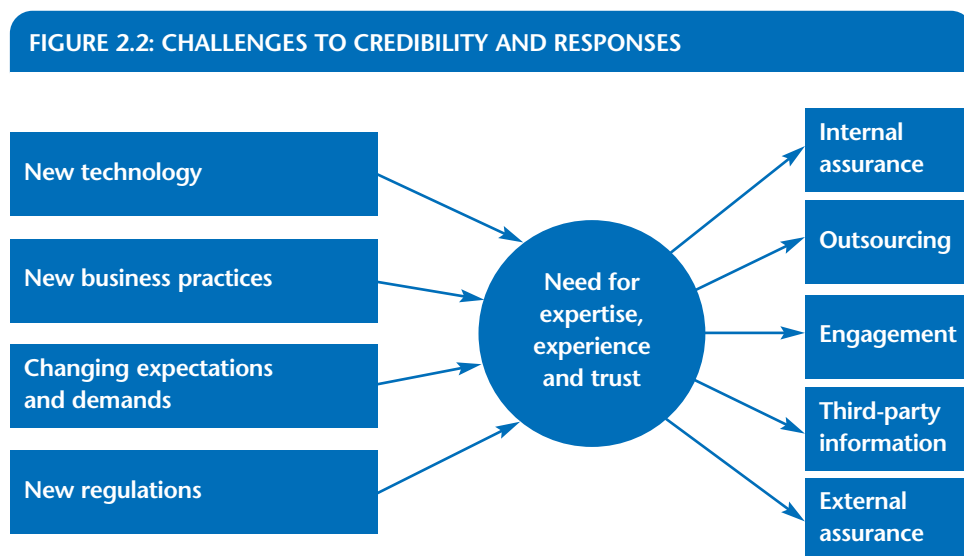
In being able to engage with businesses, stakeholders may also have the ability to demand additional information where necessary or to influence policies and decisions taken by businesses. These relationships help stakeholders gain a better understanding and knowledge of businesses and how they operate.

There are, however, other external sources (third-party information) which stakeholders might use to assess the reliability of information. For example, service industries like the restaurant trade rely heavily on reputation to attract customers. Customers will use information from food critics, restaurant guides and experiences of friends and family to decide whether to eat in a particular restaurant or not. The internet also provides useful sources of information to stakeholders.

Some markets have thrived by providing people with access to reliable information. E-bay is a good example of a market that has developed and flourished by establishing trust. E-bay relies heavily on feedback from market participants about the integrity of suppliers and customers in completing transactions. Businesses might also seek to gain credibility and enhance their reputation through gaining credentials such as awards or certificates and competitors might expose the poor quality of businesses' products or information through advertising campaigns. There are also other ways of assessing information, for example, through externally compiled industry benchmarking data.

External assurance is another solution and is considered in section 3.

Building on the model in figure 2.1 the solutions might be presented as follows:



Businesses might choose more than one solution. For example, stakeholders may look for both effective internal controls and external assurance to meet their needs. One key difference, however, between some of the solutions outlined above and external assurance will often be independence. An external assurance service, as discussed in this paper, is carried out by an expert satisfying published independence criteria.

QUESTIONS FOR DISCUSSION

1. This paper explains the different ways that business and their stakeholders can build trust in the credibility of information. Which of these potential solutions do you use and why?

3. What is external assurance?

A dictionary definition of the word ‘assurance’ is ‘a positive declaration intended to give confidence’.³ When applied in the context of business information, external assurance may be described as the provision of an independent opinion by an expert practitioner (such as a chartered accountant) on information prepared by one party for the benefit of another party or parties.

It is important to emphasise the point that the opinion comes from an independent source. Stakeholders want credible information that they can trust. Objectivity and independence are therefore essential characteristics of external assurance. Practitioners who perform assurance engagements by applying the International Auditing and Assurance Standards Board *International Framework for Assurance Engagements* (the IAASB Framework) are governed by a code of ethics which includes requirements regarding independence and maintaining professional competence.⁴ The IAASB Framework is discussed in more detail in section 5.

Another important characteristic is that of professional judgement. Practitioners need to have the ability to make professional judgements that are ethical and apply relevant knowledge to specific situations. It is essential to have the ability to understand and assess the reliability of information and to have the strength of character to challenge management where concerns arise.

There is a wide range of information in the market, which could be subject to some form of external assurance. Areas where an external assurance service might be requested include:

- quantitative information, including financial information;
- internal controls;
- environmental statements;
- compliance with contractual agreements;
- outsourced operations/service organisations;
- narrative information;
- corporate governance performance; and
- human resource performance indicators.

The following examples illustrate how external assurance can help to reinforce relationships of trust and ensure that information flows are relevant and reliable.

Some information is highly detailed and technically complex, for example, non-financial information provided in environmental reports or included in the annual report and accounts. Businesses may need external expertise to help ensure that this information is reliable and fit for its intended purpose. Likewise, stakeholders want objective information and may be concerned that businesses are putting too positive an angle on information provided in, for example, their operating and financial review. External assurance may be able to help with this.

The use of outsourced services can present concerns around objectivity and the reliability of information or internal controls. One potential solution for businesses is to have an

³ *Concise Oxford English Dictionary*, Oxford: Oxford University Press, 2004.

⁴ IAASB functions as an independent standard setting body under the auspices of the International Federation of Accountants (IFAC). The ICAEW is a member body of IFAC and is committed to supporting its work.

independent expert, a practitioner, check the reliability of information provided or the activities or the contractual compliance of the service provider. These are forms of external assurance.

There are other reasons why certain stakeholders might seek some form of external assurance over information provided to them. For example, in regulated business sectors an external assurance service might be one of the ways available to regulators to help them ensure that these entities are complying with specific requirements.

You may know of other examples where external assurance has increased trust amongst stakeholders. We are keen to hear about your own experiences and any views on the role of external assurance in complementing businesses' own internal processes.

QUESTIONS FOR DISCUSSION

2. External assurance may be described as the provision of an independent opinion provided by an expert practitioner on information prepared by business for the benefit of stakeholders. On what types of information do you seek external assurance and why?
3. Can you provide examples of circumstances where external assurance has helped to reinforce trust?
4. Are there types of information on which you would like external assurance that is not currently available?

4. Practical issues

There are a number of practical issues concerning the provision of external assurance services. Section 2.2 has already highlighted that there are a number of ways of building trust in the credibility of information, other than external assurance. There is also a lack of common understanding about what is meant by external assurance. This is clear from the expectation gaps that arise even in relation to the most long-established of external assurance services, the statutory audit of financial statements. For example, there can be confusion over who the users are, the nature and scope of work involved and what is meant by the opinion provided.

Even though there is no clear understanding of what is meant by external assurance, some external assurance services have developed in the market place and these provide a range of different types of external assurance report and conclusions. A number of practitioners (such as chartered accountants) provide these services but there are also a variety of other providers. A diversity of reports might not be an issue where the reports meet specific stakeholder needs and satisfy different audiences for different purposes but if one set of stakeholders receives different types of reports from different businesses then it might be difficult to make comparisons.

Whilst external assurance has an important role to play there is a need for realistic expectations. Some may think that practitioners are there primarily to identify and resolve problems within the business, for example with systems and controls, can give comfort over the future prospects of the business or that an assurance report on one aspect of the business somehow gives them comfort over the whole business. This is not the case. External assurance is about practitioners giving a professional opinion on information. The work performed might be subject to challenge where there is dissatisfaction with its quality but external assurance should not be seen as an insurance policy, i.e. a source of recourse when something goes wrong with the business.

Practitioners also, therefore, need to assess and manage their risks when taking on an external assurance engagement and this includes only doing what they believe they are competent to do. They would only provide an external assurance service where they have considered the risk/reward and, where appropriate, have communicated to the client and other stakeholders the limitations of what can be done in the circumstances.

QUESTIONS FOR DISCUSSION

5. The paper indicates that there are a number of different practitioners who provide external assurance reports. Who provides the external assurance reports you use and how do you satisfy yourself about the quality of these reports?
6. The paper highlights that there are a number of different external assurance reports being provided. What types of conclusions are included in external assurance reports you commission or use and are they meeting your needs?
7. Have you experienced difficulties in trying to compare external assurance reports and if so, how have you addressed these concerns?

5. Frameworks for external assurance services

Potential confusion about what is being provided and expectation gaps are driving forces behind the development of frameworks for external assurance services. An accepted framework for practitioners might help to improve consistency of reporting for external assurance services.

Many practitioners in the accounting profession may choose to follow the IAASB Framework, which was published in 2004. It is designed to be conceptually consistent with the model used for financial statement audits performed under International Standards on Auditing and is applicable to all assurance engagements. The IAASB Framework sets out high-level principles applicable to assurance engagements. The IAASB has also published International Standard on Assurance Engagements 3000, *Assurance engagements other than audits or reviews of historical financial information (ISAE 3000)*, which is also consistent with the IAASB Framework and provides guidance to practitioners on performing assurance engagements other than audits or reviews of historical financial information.

Practitioners who perform assurance engagements by applying the Framework are governed by the International Federation of Accountants (IFAC) *Code of Ethics for Professional Accountants*.⁵ The Code requires practitioners to be independent of assurance clients.

The IAASB Framework defines an assurance engagement as:

‘an engagement in which a **practitioner** expresses a conclusion designed to enhance the degree of confidence of the **intended users** other than the **responsible party** about the outcome of the evaluation or measurement of a **subject matter** against **criteria**.’

The terms which we have highlighted in bold above are discussed below.

If a stakeholder (the intended user of information) wants some assurance over information (subject matter/subject matter information) provided to them by another party (the responsible party) then an assurance engagement can be requested. An independent party (the practitioner) will perform work to obtain comfort over that information (which is measured against suitable criteria) and this comfort would then be expressed in a report as a conclusion. This conclusion is designed to enhance the confidence of the users about the information provided.

If a conclusion is not requested then it will not be an assurance engagement. For example, a factual report that just highlights the outcome of a series of tests and leaves stakeholders to derive their own conclusions (known as an ‘agreed upon procedures’ engagement) is not an assurance engagement. Other examples of services provided that are not assurance engagements include the preparation of tax returns and consultancy services.

The UK statutory audit of financial statements is an example of an assurance engagement:

- practitioners are the auditors;
- intended users are the shareholders;
- responsible party is the board of directors of the company;
- subject matter is the financial position of the company and the subject matter information is the financial statements; and
- criteria is the applicable financial reporting framework.

⁵ *Code of Ethics for Professional Accountants*, New York: IFAC, 2005.

This is just a brief overview of the IAASB Framework. Those interested in reading more about the IAASB Framework and the key elements of an assurance engagement may want to look at *Perspectives on assurance: Engaging practitioners*. That discussion paper is primarily aimed at practitioners and provides a more detailed explanation of the IAASB Framework.

The ICAEW has also issued the following guidance which is consistent with the IAASB Framework:

- Technical Release AAF 01/06, *Assurance reports on internal controls of service organisations made available to third parties*;
- Technical Release ITF 01/07, *Assurance report on the outsourced provision of information services and information processing services*; and
- Interim Technical Release, AAF 03/06, *The ICAEW assurance service on unaudited financial statements*.

QUESTIONS FOR DISCUSSION

8. For specific types of external assurance report, do you know whether the practitioner has followed a particular framework? If so, what was the framework and was it helpful to know that it had been applied?

Appendix – References

Institute of Chartered Accountants in England and Wales

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December 2007