SA402 : Audit considerations related to Entity
using a Service Organisation

payroll accounting

Service affects F.R.
↓
Relevant to Audit

(Client) **Mentor Graphics**
[User Entity] — ICs ✓

DKM Solutions (Service Org.)
ICs ✓ S.O.

Security guard service
F.R. process
Audit

I. Service Relevant to F.R? ⟶ **SA402** II. Understand Service → III. Take Type 1 or 2 Reports to support understanding
↓
V. Reporting. ⟵ IV. Test of controls.
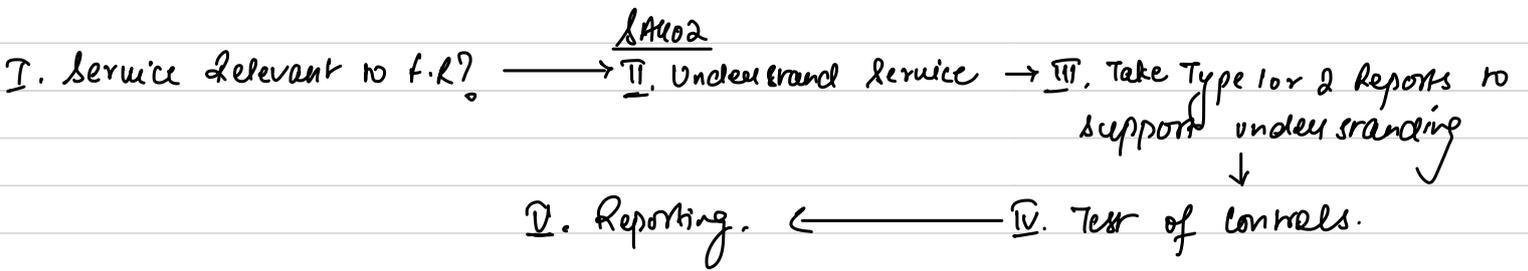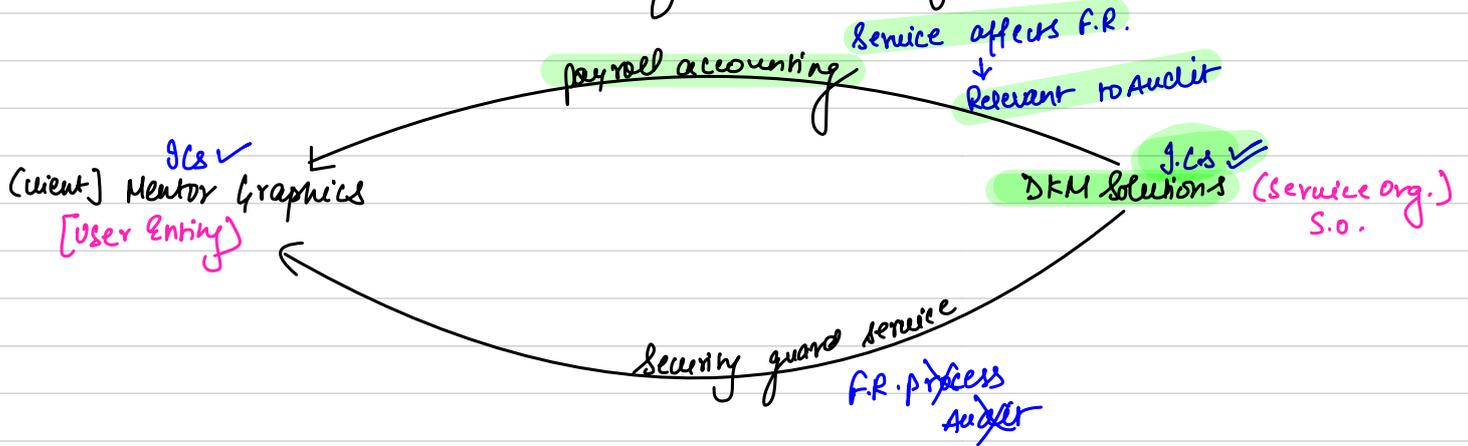
Q How to know if SO's services are relevant to User Entity's F.R. process?

SO's services are relevant to user entity's F.R. process, if services affect any of following:

[Trans^n I & IC → Recorded, posted, rectified → F.S.prepared → Adj. Entries]

① SCOTs : Significant Class of Trans^n eg Revenue/Purchases etc.

② How Info. system captures Event/Cond^n other than SCoTs.

③ Procedures

④ A/c Records

[Manual/Automated) in which Trans^n are Initiated, recorded, processed, rectified, tofd. to G.L. & reported in FS.

⑤ Financial Reporting Process to prepare FS.

⑥ Controls Surrounding JEs Including non-standard JEs ie ⎨ Non-Recurring / Unusual / Adjustment Entries.

ANU

**Q** Obtaining understanding of services of S.O.

a) **Nature & significance** of service to user entity.

Can obtain info. from contract, user manuals, reports of service auditor etc.
(Soon)

b) **Nature & materiality** of transⁿ processed by S.O.

eg payroll A/c service [significant] → process Employee benefit app. [Material]

c) **Degree** of **interaction** b/w user entity & S.O. Activities.

user Entity —— Sends data ——→ S.O.
[Authorise] ←—— Accounting.
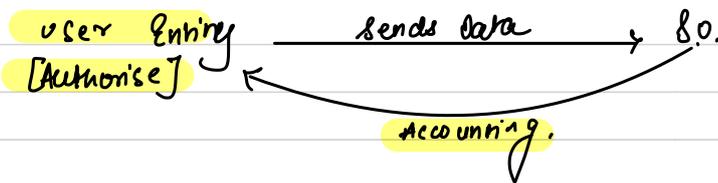
d) **Nature** of **relationship** b/w user entity & S.O. Including contractual terms.

dwins °°✓

Understanding ? ○ User Entity
[from where]
[or]
• contract S.O. through user entity.
• visit S.O.
• using another auditor to perform procedures.
• obtain Type 1 or 2 Report

user Entity   S.O.
• payroll Accounting service
↓
Report on S.C.S. [Type 1 or 2].
& Service Auditor

2 Types of Reports

Type 1

- S.O's description of System.
- written assertion by S.O. :

S.O's system described **fairly**.

controls related to control objectives are **Suitably designed**.

at a **specified date**.

- Service Auditor's Assurance Report giving **Reasonable Assurance** on above matters.

Type 2

- S.O's description of System.
- written assertion by S.O. :

S.O's system described **fairly**.

controls related to control objectives are **Suitably designed**.

controls operated effectively

throughout specified period.

- Service Auditor's Assurance Report giving **Reasonable Assurance** on above matters.

(+)

Description of [ToCs + Results].

Q. Using a Type 1 or 2 Report → Support user auditor's understanding of S.O.

be **Satisfied** about ☞ Service Auditor's ⎯ **Independence** for S.O.
⎯ **Competence** [except for CA].
↓
Adequacy of standards under which Type 1 or 2
[SAE 3402] report issued.

User auditor shall evaluate :

- Description & design of **controls at S.O.** [at a date / appt. period]. Type 1   Type 2

- **SAAE** obtained for **user entity's controls** relevant for audit.

- **complementary user entity's controls** identified by SO?
↓
(Yes)
Understand if user entity has designed & implemented such controls.

Payroll Process.

support

I. User Entity Controls.

Authorise:
- New joiner.
- Salary / Compensation.
- Increment
- Leaves the Co.

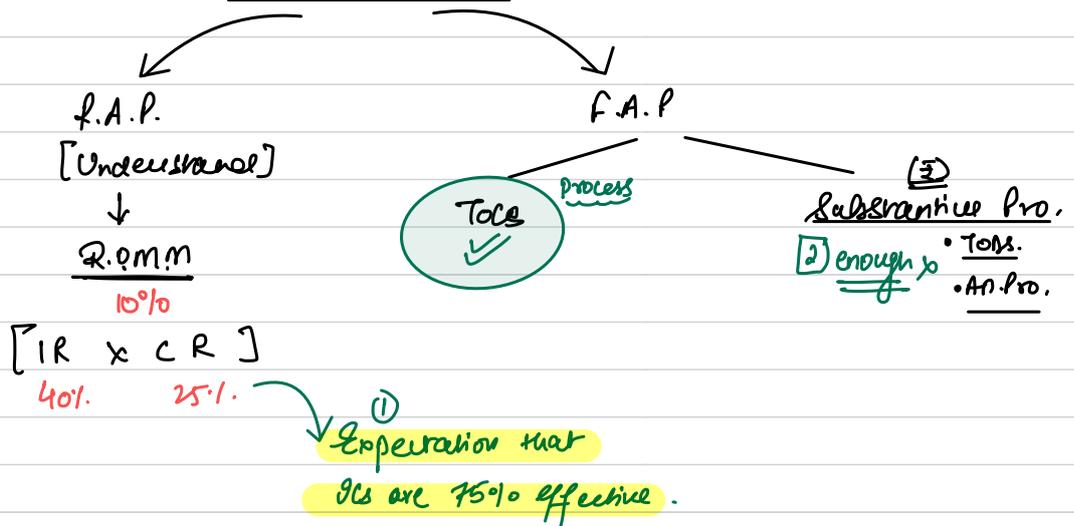**II. S.O. [Payroll Accounting]**

- monthly payroll calculation

- Deductions
  EPF | ESI | TDS

III. Complementary User Entity Controls.

- Send payroll data for processing on time

- Review payroll registers. & communicate errors. to S.O.
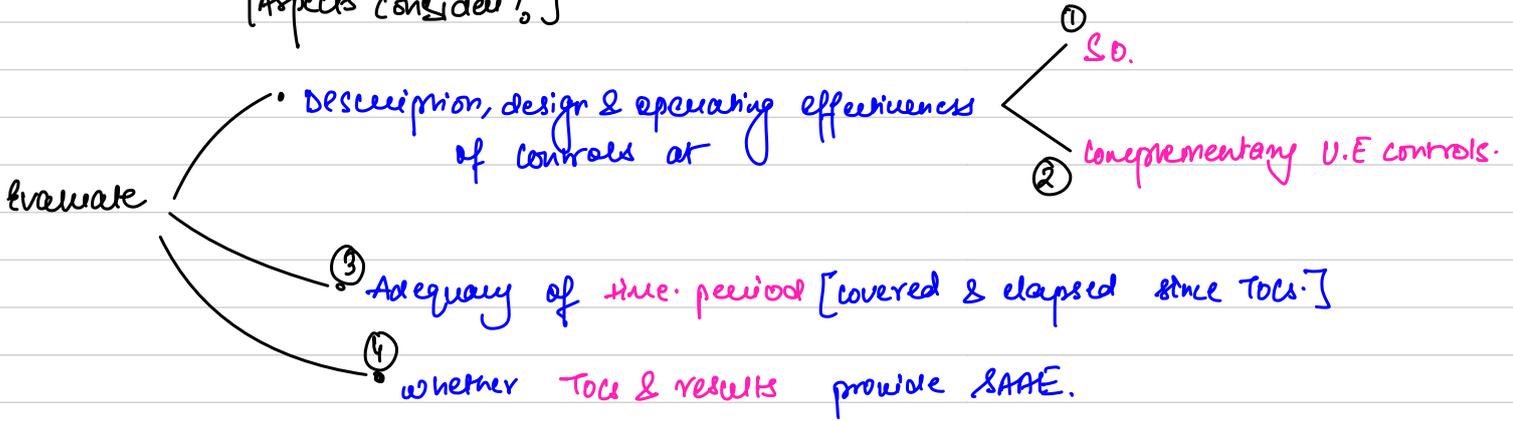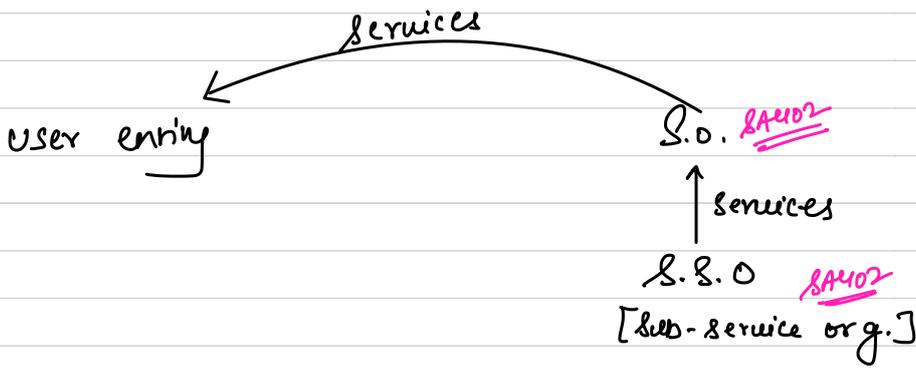

Q Why we do. TOCs ?

A. Procedures

R.A.P.
[Understand]
↓
R.o.m.m
10%

[IR × CR]
40%   25%

① Expectation that ICs are 75% effective.

F.A.P

TOCs ✓   Process

(3) Substantive Pro.
② enough to
- TODs.
- An.Pro.

Using Type 2 Report to obtain evidence
for operating effectiveness of controls.

[Aspects considered?]

Evaluate
- Description, design & operating effectiveness of controls at
  - ① S.O.
  - ② complementary U.E controls.
- ③ Adequacy of time. period [covered & elapsed since TOCs.]
- ④ whether TOC & results provide SAAE.

during :)

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services

user entity ←——— S.O. SA402

↑ services

S.S.O SA402
[Sub-service org.]

Service auditor ——→ Type 1 or 2 Report [Controls at S.O.]
↓
S.S.O

Include   Exclude.
Inclusive method   carve-out method :)

:)   SA402 [S.S.O]
                                - contact
                                - visit
                                - Another auditor
                                - Type 1 or 2 Report.
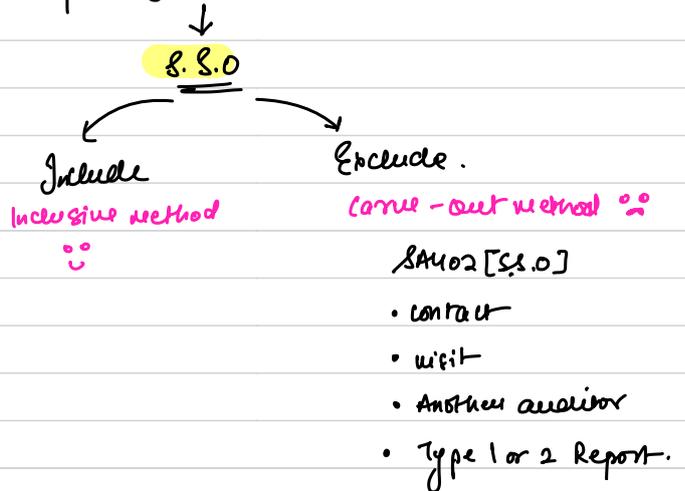
SA402: Audit considerations for User Entity using a S.O.

1. **S.O. Services relevant to user entity's FR process**

   - Trans^n — SCOTs
     - How info. system captures ELC^n
   - Procedures } manual/
   - A/c Records } automated
   - F.R.P (Prepare FS)
   - Non std JEs (ANU)

2. **Understanding Nature & Extent of Services of S.O.**

   - Nature & significance of services
   - Nature & materiality of Trans^n
   - Degree of interaction
   - Nature of Relationship

3. **Understanding → How?** • user entity →→ contact S.O. /visit / another auditor / Type 1/2 Report.

   Type 1 Report ⇒ Description of system + SO's Assertion (fair description + controls designed) → Date.
   + R.A. Report

   Type 2 Report ⇒ Description of system + SO's assertion (fair description + controls designed + op. effer.)
   + R.A. (+ TOCs & Results)   throughout period.

   ⇒ **Using Type 1/2 Reports to support understanding of S.O.**

   Be satisfied [@ Service Auditor (competence, independence, stds.) + Evaluate ┌ D&D of S.O. controls ← Date ─ period.
   ├ UE controls ⇒ SAAE?
   └ Comp. UE controls identified
     ↳ D & implement?

4. **TOCs (why?)** ⇒ Expectation controls operating effectively
   ↓
   S.O. [Type 2 / Test / other auditor)

5. **[Type 2] Report → SAAE for op. effectiveness of controls → Aspects?**

   Description, design & op. effectiveness ┌ SO   + Period   + TOCs & Results
   of controls   └ Comp. UE controls   (covered elapsed)   (SAAE?)

6. Fraud, NOCLAA, un corrected misst. at S.O. → Inquire! → NTE of FAP + Reporting/concern

7. A. Report ──→ unmodified opinion → Refer ✗
   ↓
   modified opinion (Relevant) ──→ Refer ✓