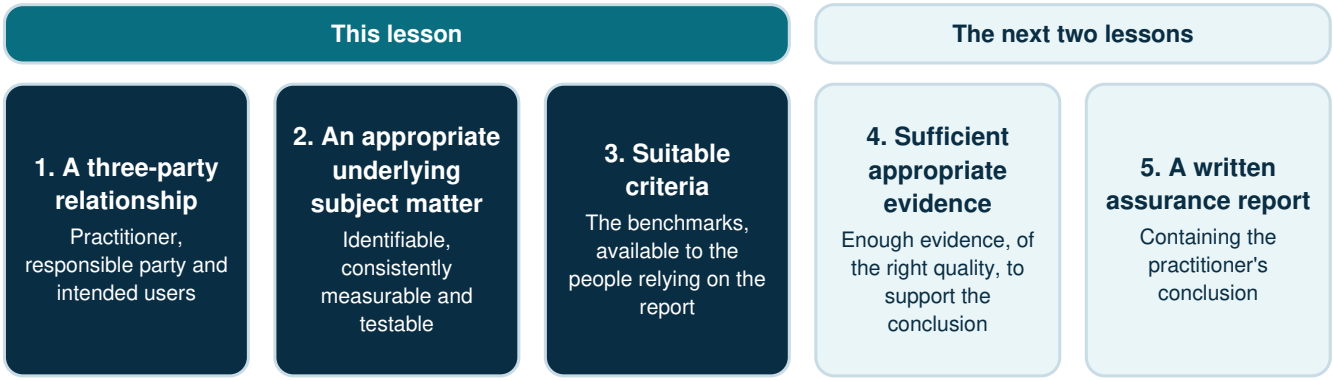
Three parties, subject matter and criteria

MODULE 1 | 1.2.6 | STUDENT COMPANION

Every assurance engagement needs **five elements**. This lesson covers the first three: a **three-party relationship**, an **appropriate underlying subject matter**, and **suitable criteria** that are available to the people relying on the report. Criteria matter more than they look: two honest organisations can measure exactly the same activity and report very different numbers.

The five elements of an assurance engagement



If any element is missing, the work may still be valuable, but it isn't an assurance engagement

The parties

These roles can be held by the same party or by different parties.

Role	Who it is
Practitioner	The person or firm doing the assurance work and giving the conclusion
Responsible party	Whoever is responsible for the underlying subject matter; in a financial statement audit, normally the board of directors
Intended users	The people the report is written for, such as shareholders, lenders and other providers of capital
Engaging party (sometimes separate)	Whoever engages the practitioner
Measurer or evaluator (sometimes separate)	Whoever applies the criteria to the subject matter, such as a company's finance team

- **Two limits always apply.** The practitioner can never be the responsible party, because nobody can independently assure their own information. The responsible party can be one of the intended users, but never the only one, or the report would only tell its preparer what it already knows.

- **Restricted use:** when a report is written for one user and one purpose, such as a bank's covenant report, the practitioner may restrict its use to that user, so that others don't rely on it for purposes it wasn't designed for.

Who's who in three engagements

Role	Company audit	Bank covenant report	Second Helping meals report
Practitioner	The auditor	An assurance practitioner	An assurance practitioner
Responsible party	The board of directors	The company	Second Helping (its board)
Measurer or evaluator	The finance team, preparing the statements	The company's finance team, measuring covenant compliance	Charity staff, weighing deliveries and converting them to meals
Engaging party	The company, which appoints its auditor	The company	Second Helping
Intended users	Shareholders, lenders and other providers of capital	The bank (use of the report can be restricted to it)	Major donors and the government grant body

An appropriate underlying subject matter

The subject matter is appropriate when it can be **identified**, when it can be **consistently measured or evaluated** against the criteria, and when the resulting information can be put through procedures that produce **sufficient appropriate evidence**. Non-financial subject matter is often trickier: it mixes numbers with narrative, and it rarely has measurement rules as developed as the accounting standards.

Forms the subject matter can take

Form	Example (imagined)
Financial performance or position	A franchise network's monthly sales
Non-financial performance	An internet provider's average time to answer support calls
Physical characteristics	The storage capacity of a grain terminal
Systems and processes	A hospital's controls over who can change patient billing records
Behaviour	A club's compliance with its liquor licence, or the conduct of a board's governance

Suitable criteria

Criteria are the benchmarks used to measure or evaluate the subject matter. **Established criteria** are set by an authoritative body through a transparent process, such as the accounting standards, or the Greenhouse Gas Protocol, the most widely used international method for measuring an organisation's emissions. **Specifically developed criteria** are designed for the engagement, by the responsible party or sometimes by the practitioner. Either way, they must be **suitable**, and **available** to the people relying on the report: a conclusion means nothing if the reader doesn't know what yardstick was used.

Second Helping (imagined), a food rescue charity, reports that it delivered 1.2 million meals last year, and its major donors and a government grant body want the figure assured. The underlying subject matter is the food redistributed; the subject matter information is the meals figure; the criteria are the charity's own rules for turning food into meals. It weighs surplus food and counts every 400 g delivered as one meal. Had it chosen 250 g a meal, the same food would have produced about 1.9 million meals.

Testing the meals count against the five qualities

The rule: every 400 g of food delivered counts as one meal, giving **1.2 million meals**. At 250 g a meal, the same food would count as **about 1.9 million**: 60% more, without one extra plate served.

Quality	The question it asks	Testing the meals count
Relevance	Do the criteria help users make their decisions?	Count food delivered to partner agencies, not food collected, some of which may never leave the warehouse
Completeness	Is anything significant left out that could affect users' conclusions?	Say how spoiled food is treated, rather than quietly dropping it or counting it anyway
Reliability	Would different people, at different times, measure it consistently?	Calibrated scales on every delivery, not drivers estimating loads by eye
Neutrality	Are the criteria free from bias?	A conversion rate from a recognised source, applied every year, not the most generous rate available
Understandability	Are they clear enough that users won't read them very differently?	Explain what a 'meal' is, rather than just reporting a number of meals

If the criteria fail: suitable criteria are a precondition for accepting an assurance engagement. If the charity's criteria were unsuitable and it wouldn't change them, the practitioner shouldn't accept the work as an assurance engagement, because no conclusion could mean what users would think it meant. More often, the practitioner's questions improve the criteria, and the charity ends up with a better, more credible measure, disclosed alongside the figure.

Practice questions

MODULE 1 | 1.2.6 | TRY THESE BEFORE THE WORKED ANSWERS

Question 1 - Who's who?

Engagement (all imagined)	Responsible party	Engaging party	Intended users
(a) Crumbworth Bakehouse, a franchisor, requires each franchisee to provide an assurance report on the monthly sales that set its royalties. Hollis Bakeries, a franchisee, engages a practitioner.			
(b) A state sports department engages a practitioner to report on whether Merrigal Rowing Club spent its $400,000 boatshed grant in line with the grant conditions.			
(c) Highcrest Air's board asks a practitioner for assurance on the airline's sustainability report, which will be published for investors, customers and community groups.			
(d) Quandong Capital, planning to buy Coolabah Fitness, engages a practitioner to give assurance on the gym chain's reported membership numbers.			

Question 2 - Appropriate subject matter?

Tumbarra Regional Gallery (imagined) is considering three subject matters for an assurance engagement. Decide whether each is appropriate, and explain why.

Proposed subject matter	Appropriate?	Why
(a) The number of visitors last year, counted by electronic sensors at both entrances		
(b) How much visitors loved the new exhibition		
(c) The gallery's compliance with its child-safety policy for school group visits		

Question 3 - Test the pothole criteria

Ardley Shire Council (imagined) reports that 92% of potholes were repaired within five working days. Its criteria: (1) the clock starts when a works crew logs the pothole in the council's system, not when a resident reports it; (2) a temporary cold-mix patch counts as a repair; (3) potholes on state-managed roads are excluded, and after-hours reports aren't logged until staff return; (4) crews record repair dates on paper sheets, typed in once a week; (5) the report doesn't define a pothole or mention any of these rules. Test the criteria against the five qualities.

Quality	Your assessment
Relevance	
Completeness	
Reliability	
Neutrality	
Understandability	

Worked answers

MODULE 1 | 1.2.6 | WORKED ANSWERS - ATTEMPT THE QUESTIONS FIRST

Question 1 - Parties (sample answer)

Engagement	Responsible party	Engaging party	Intended users
(a) Franchise sales	Hollis Bakeries (its directors)	Hollis Bakeries	Crumbworth Bakehouse, the franchisor
(b) Boatshed grant	Merrigal Rowing Club (its committee)	The state sports department	The department, and possibly the club's members
(c) Sustainability report	Highcrest Air (its board)	Highcrest Air's board	Investors, customers and community groups
(d) Membership numbers	Coolabah Fitness (its directors)	Quandong Capital	Quandong Capital, and perhaps its lenders

Question 2 - Tumbarra Regional Gallery (sample answer)

Subject matter	Appropriate?	Why
(a) Visitor numbers	Yes	Identifiable and consistently measurable, with evidence available (sensor logs, calibration checks, reconciliation to ticket sales). Criteria must cover re-entries
(b) How much visitors loved it	No, as stated	'Loved' can't be measured consistently. It could become appropriate if redefined, such as the share of exit-survey ratings of 4 or 5 out of 5
(c) Child-safety compliance	Yes	Behaviour measured against a written policy, with evidence from booking records, staff screening checks, supervision ratios and incident logs

Question 3 - Ardley Shire Council (sample answer)

Quality	Assessment
Relevance	Residents care about the time from their report to a proper repair; a crew-logged start and a temporary patch as the finish make the figure less relevant
Completeness	After-hours delays and permanent repairs are left out. Excluding state roads may be reasonable, but only if disclosed
Reliability	Paper sheets typed in weekly invite errors and inconsistency. System timestamps for the report and the repair would be more reliable
Neutrality	Every choice flatters the result: a later start, an earlier finish, helpful exclusions. Neutral criteria would run from the resident's report to the permanent repair
Understandability	With no definition or disclosed rules, readers will assume potholes were fully fixed within five days of being reported; the criteria must be disclosed