

TERM	DEFINITION
Audit Terms	
User Organization	The entity that has engaged a service organization and whose financial statements are being audited.
User Auditor	The auditor who reports on the financial statements of the user organization.
Service Organization	The entity (or segment of an entity) that provides services to a user organization that may be relevant to a user organization's internal control as it relates to an audit of financial statements.
Service Auditor	The auditor who reports on controls of a service organization that may be relevant to a user organization's internal control as it relates to an audit of financial statements.
Service Auditor's Report	A service auditor's report on a service organization's description of its controls that may be relevant to a user organization's internal control as it relates to an audit of financial statements. It is also known as a SAS 70 report.
Type I SAS 70 Report <i>(a.k.a. Report on Controls Placed in Operation)</i>	A service auditor's report on a service organization's description of its controls that may be relevant to a user organization's internal control as it relates to an audit of financial statements, on whether such controls were suitably designed to achieve specified control objectives, and on whether they had been placed in operation as of a specific date. Such reports may be useful in providing a user auditor with an understanding of the controls necessary to plan the audit and to design effective tests of controls and substantive tests at the user organization, but they are not intended to provide the user auditor with a basis for reducing his or her assessments of control risk below the maximum.
Type II SAS 70 Report <i>(a.k.a. Report on Controls Placed in Operation and Tests of Operating Effectiveness)</i>	A service auditor's report on a service organization's description of its controls that may be relevant to a user organization's internal control as it relates to an audit of financial statements, on whether such controls were suitably designed to achieve specified control objectives, on whether they had been placed in operation as of a specific date, and on whether the controls that were tested were operating with sufficient effectiveness to provide reasonable, but not absolute, assurance that the related control objectives were achieved during the period specified. Such reports may be useful in providing the user auditor with an understanding of the controls necessary to plan the audit and may also provide the user auditor with a basis for reducing his or her assessments of control risk below the maximum.
Controls	The policies and procedures an entity establishes to implement one or more aspects of the five components of internal control. Controls that affect a user organization's financial statements may exist at the user organization or at the service organization because when a user organization uses a service organization, certain controls at the service organization may be part of the user organization's information system.
Service Organization's Controls	Controls at a service organization that may be part of a user organization's information system in the context of an audit of the user organization's financial statements. They do not include service organization controls that are not relevant to a user organization's information system.

TERM	DEFINITION
Audit Terms (cont)	
Control Objectives	Control objectives are generally financial statement reporting control objectives, but also may encompass compliance or operational control objectives.
Internal Control	Internal control is defined as a process designed to provide reasonable assurance regarding the achievement of objectives in the following categories: <ul style="list-style-type: none"> • Reliability of financial reporting; • Effectiveness and efficiency of operations; and • Compliance with applicable laws and regulations.
Control Environment	The control environment sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all the other components of internal control, providing discipline and structure. Control environment is one of the five interrelated components of internal control.
Risk Assessment	The auditor who reports on controls of a service organization that may be relevant to a user organization's internal control as it relates to an audit of financial statements.
Control Activities <i>(a.k.a. Control Procedures)</i>	Control activities are the policies and procedures that help ensure that management directives are carried out. Control activities are one of the five interrelated components of internal control.
Information and Communication	Information and communication systems support the identification, capture, and exchange of information in a form and time frame that enable people to carry out their responsibilities. Information and communication systems are one of the five interrelated components of internal control.
Internal Control Terms	
Monitoring	Monitoring is a process that assesses the quality of internal control performance over time. Monitoring is one of the five interrelated components of internal control.
Complementary User Organization	In certain circumstances, a service provided by the service organization may be designed with the assumption that certain controls will be implemented by the user organizations. For example, the service may be designed with the assumption that the user organizations will have controls in place for authorizing transactions before they are sent to the service organization for processing. If such complementary user organization controls are required to achieve the stated control objectives, the service organization should describe them in its description of controls.
Service Organization's Controls	Controls at a service organization that may be part of a user organization's information system in the context of an audit of the user organization's financial statements. They do not include service organization controls that are not relevant to a user organization's information system.

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Subservice Organization Terms	
Subservice Organizations	<p>A user organization may use a service organization that, in turn, uses another service organization, known as a subservice organization. The subservice organization may perform functions or processing that is part of the user organization’s information system as it relates to an audit of financial statements. The subservice organization may be a separate entity from the service organization or may be related to the service organization.</p>
The Carve-out Method <i>(Alternative method of reporting when the service organization utilizes a subservice organization)</i>	<p>The subservice organization’s relevant control objectives and controls are excluded from the description and from the scope of the service auditor’s engagement. The service organization states in the description that the subservice organization’s control objectives and related controls are omitted from the description and that the control objectives in the report include only the objectives the service organization’s controls are intended to achieve.</p>
The Inclusive Method <i>(Alternative method of reporting when the service organization utilizes a subservice organization)</i>	<p>The subservice organization’s relevant controls are included in the description and in the scope of the engagement. The description clearly differentiates between controls of the service organization and controls of the subservice organization. The set of control objectives includes all of the objectives a user auditor would expect both the service organization and the subservice organization to achieve. To accomplish this, the service organization coordinates the description of controls with the subservice organization.</p>

References:

- Statement on Auditing Standards (SAS) No. 70, Service Organizations, as amended.
- Statement on Auditing Standards (SAS) No. 94, The Effect of Information Technology on the Auditor’s Consideration of Internal Control in a Financial Statement Audit
- AICPA Audit Guide — Service Organizations: Applying SAS No. 70, as amended.