For CA FINAL

Group I – PAPER 3

ADVANCE AUDITING ASSURANCE

AND

PROFESSIONAL ETHICS

VOLUME – I (A)

ENGAGEMENT STANDARDS

Edition – 10

New Syllabus

KEY FEATURES:

- ✓ Based on the Institute's New Module
- ✓ Updated Outline of the Chapters
- ✓ OFUs for Understanding Technical Concepts
- ✓ Compiled Question Bank: Theoretical, RTP and MCQs
- ✓ All Answers in Point Form – Easy to grasp & understand
- ✓ Simple and Lucid Language

CA CS Amit Tated

FCA, CS, DISA

For C.A. Final

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We express our sincere thanks to all our readers, authors and business associates for helping us in our mission of producing quality books for quality education. We wish all our young readers a brilliant success in various examinations and a bright future.

- Publisher

VISION:

To provide simple yet standardized, short yet complete, conceptual yet affordable, education to students enhancing their knowledge from heart & mind.

MISSION:

Providing personalized and affordable coaching and support of best possible standard, in shortest possible time.

CA. AMIT TATED

Founder: A. T. Academy

Preface

It gives me immense pleasure to present the Tenth Revised edition of Advanced Auditing, Assurance & Professional Ethics. This edition has updated syllabus which is applicable from November 2024 Exams and onwards.

This book has everything which student may require to understand, remember and reproduce Audit. The book has been developed keeping in mind the technicality of the subject to bring it at a student's grasping level.

This book will suffice to go with institute language as well as understanding the concept.

In recent exam papers we saw that the questions asked are more practical. Thus, students need to understand the concepts and logical reasoning of the Chapter. Only mugging-up shall not suffice to score in this subject.

For Class Work students can refer Amit Tated YouTube Channel.
(Tera Course Mera Guidance)

Every effort has been made to avoid any errors and omissions in this book. Despite all the efforts we believe some errors might have crept in. The students are welcome to point out any errors / suggestions.

Best wishes,

Amit Tated
(atacademyforca@gmail.com)

August, 2024

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I would like to acknowledge my Parents (Vijay & Shobha), Manish, Allan, Ritesh, Bhavesh & Sumeet for all their support towards my journey of studies, career & experience.

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1. QUALITY CONTROL

1. AUDIT QUALITY

SQC 1- Quality Control for firms that perform audits and reviews of historical financial information, and other assurance and related services engagements and SA-220- Quality Control for an audit of financial statements deal with issue of establishing quality control systems and responsibilities of auditors in this regard. Both the standards deal with framework of audit quality.

2. SQC 1 - QUALITY CONTROL FOR FIRMS THAT PERFORM AUDITS AND REVIEWS OF HISTORICAL FINANCIAL INFORMATION, AND OTHER ASSURANCE AND RELATED SERVICES ENGAGEMENTS

2.1 Elements of System of Quality Control

The firm's system of quality control should include policies and procedures addressing each of the following elements: -

2.1.1 Leadership Responsibilities for Quality within the Firm

SQC 1 requires firms to establish policies and procedures designed to promote an internal culture based on the recognition that quality is essential in performing engagements. Such policies and procedures should require the firm's chief executive officer or the firm's managing partners to assume ultimate responsibility for the firm's system of quality control. The example set by firm's leadership encourages an inner culture that recognizes high quality audit work. Further, persons assigned operational responsibilities for the firm's quality control system by the firm's chief executive officer or managing partners should have sufficient and appropriate experience, ability, and the necessary authority to assume that responsibility.

It has been laid down clearly that firm's business strategy is subject to the overriding requirement for the firm to achieve quality in all the engagements that the firm performs. Essentially, it implies that audit quality is paramount in all engagements. It is non-negotiable. In this regard, it should be ensured that: -

(a) The firm assigns its management responsibilities so that commercial considerations do not override the quality of work performed.

(b) The firm's policies and procedures addressing performance evaluation, compensation, and promotion (including incentive systems) with regard to its personnel are designed to demonstrate the firm's overriding commitment to quality and

(c) The firm devotes sufficient resources for the development, documentation and support of its quality control policies and procedures.

2.1.2 Ethical Requirements

The Code establishes the fundamental principles of professional ethics which include integrity, objectivity, professional competence and due care, confidentiality and professional behaviour. Fundamental principles should be emphasized by

- Actions of the leadership of the firm
- Spreading awareness and training
- Monitoring
- A process for dealing with non-compliance.

Such policies and procedures should enable the firm to: -

(a) Communicate its independence requirements to its personnel

(b) Identify and evaluate circumstances and relationships that create threats to independence, and to take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the engagement.

(c) There should exist a mechanism in the firm by which engagement partners provide the firm with relevant information about client engagements and personnel of firm promptly notify firm of circumstances and relationships that create a threat to independence. All breaches of independence should be promptly notified to firm for appropriate action.

(d) At least annually, the firm should obtain written confirmation of compliance.

SQC 1 lays special emphasis: Using the same senior personnel on assurance engagements over a prolonged period may impair the quality of performance of the engagement. In determining appropriate criteria, the firm considers such matters as-

(a)	the nature of the engagement, including the extent to which it involves a matter of public interest and
(b)	the length of service of the senior personnel on the engagement.

Examples of safeguards include rotating the senior personnel or requiring an engagement quality control review. The familiarity threat is particularly relevant in the context of financial statement audits of listed entities. For these audits, the engagement partner should be rotated after a pre- defined period, normally not more than seven years (except in cases where audit of listed entities is conducted by a sole practitioner).

2.1.3 Acceptance and Continuance of Client Relationships and Specific Engagements

A firm before accepting an engagement should acquire vital information about the client. Such an information should help firm to decide about:-

- Integrity of Client, promoters and key managerial personnel.
- Competence (including capabilities, time and resources) to perform engagement.
- Compliance with ethical requirements.

❖ **With regard to the integrity of a client, matters that the firm considers include, for example**

The identity and business reputation of the client's principal owners, key management, related parties and those charged with its governance.

- The nature of the client's operations, including its business practices
- Information concerning the attitude of the client's principal owners, key management and those charged with its governance towards such matters as aggressive interpretation of accounting standards and the internal control environment.
- Whether the client is aggressively concerned with maintaining the firm's fees as low as possible.
- Indications of an inappropriate limitation in the scope of work.
- Indications that the client might be involved in money laundering or other criminal activities.
- The reasons for the proposed appointment of the firm and non-reappointment of the previous firm.

❖ **In considering whether the firm has the capabilities, competence, time and resource undertake an engagement, following matters have to be taken into consideration: -**

- Firm personnel have knowledge of relevant industries or subject matters;
- Firm personnel have experience with relevant regulatory or reporting requirements, or the ability to gain the necessary skills and knowledge effectively;
- The firm has sufficient personnel with the necessary capabilities and competence;
- Experts are available, if needed;
- Individuals meeting the criteria and eligibility requirements to perform engagement quality control review are available, where applicable; and
- The firm would be able to complete the engagement within the reporting deadline.

Where the firm obtains information that would have caused it to decline an engagement if that information had been obtainable earlier, policies and procedures on the continuance of the engagement and the client relationship should include consideration of:

(a) The professional and legal responsibilities that apply to the circumstances, including whether there is a requirement for the firm to report to the person or persons who made the appointment or, in some cases, to regulatory authorities; and

(b) The possibility of withdrawing from the engagement or from both the engagement and the client relationship.

❖ **Policies and procedures on withdrawal from an engagement or from both the engagement and the client relationship address issues that include the following:**

- Discussing with the appropriate level of the client's management and those charged with its governance regarding the appropriate action that the firm might take based on the relevant facts and circumstances.
- If the firm determines that it is appropriate to withdraw, discussing with the appropriate level of the client's management and those charged with its governance withdrawal from the engagement or from both the engagement and the client relationship, and the reasons for the withdrawal.
- Considering whether there is a professional, regulatory or legal requirement for the

firm to remain in place, or for the firm to report the withdrawal from the engagement, or from both the engagement and the client relationship, together with the reasons for the withdrawal, to regulatory authorities.

- Documenting significant issues, consultations, conclusions and the basis for the conclusions.

2.1.4 Human Resources

Such policies and procedures should address relevant HR issues including recruitment, compensation, training, career development, performance evaluation etc. There should be emphasis on the continuing professional development of firm's personnel.

The firm should establish policies and procedures requiring that:

(a) The identity and role of the engagement partner are communicated to key members of the client's management and those charged with governance;

(b) The engagement partner has the appropriate capabilities, competence, authority and time to perform the role; and

(c) The responsibilities of the engagement partner are clearly defined and communicated to that partner

2.1.5 Engagement Performance

Consistency in quality of engagement performance is achieved through briefing of engagement teams of their objectives, processes for complying with engagement standards, processes of engagement supervision and training, methods of reviewing performance of work, appropriate documentation of work performed.

❖ **Consultation in difficult or contentious matters:** Consultation includes discussion, at the appropriate professional level, with individuals within or outside the firm who have specialized expertise, to resolve a difficult or contentious matter. It helps to promote quality & improves the application of professional judgment. Consultation procedures require consultation with those having appropriate knowledge, seniority & experience within the firm (or outside the firm) on significant technical, ethical & other matters & appropriate documentation & implementation of conclusions resulting from consultations.

A firm needing to consult externally, for example, a firm without appropriate internal resources, may take advantage of advisory services provided by other firms or professional and regulatory bodies. Complete and proper documentation should be maintained on issues involved and results of consultation.

❖ ***Engagement quality control review:*** *Significant judgments made in an engagement should be reviewed by an engagement quality control reviewer for taking an objective view before the report is issued.*

The review does not reduce the responsibilities of the engagement partner.

Engagement quality control review is mandatory for all audits of financial statements of listed entities. In respect of other engagements, firm should devise criteria to determine cases requiring performance of engagement quality control review.

❖ ***An engagement quality control review for audits of financial statements of listed entities includes considering the following: -***

- *The engagement team's evaluation of the firm's independence.*
- *Significant risks identified during the engagement and the responses to those risks.*
- *Judgments made, particularly with respect to materiality and significant risks.*
- *Whether appropriate consultation has taken place.*
- *The significance and disposition of corrected and uncorrected misstatements identified during the engagement.*
- *The matters to be communicated to management and those charged with governance.*
- *Whether working papers selected for review reflect the work performed in relation to the significant judgments and support the conclusions reached.*
- *The appropriateness of the report to be issued.*

Engagement quality control reviewer is a partner, other person in the firm (who should be member of ICAI), suitably qualified external person, or a team made up of such individuals. In this regard, suitably qualified external person refers to an individual outside the firm with the capabilities and competence to act as an engagement partner, for example a partner or an employee (with appropriate experience) of another firm.

In addition, the engagement quality control reviewer for an audit of the financial statements of a listed entity is an individual with sufficient and appropriate experience and authority to act as an audit engagement partner on audits of financial statements of listed entities. It is necessary to maintain objectivity of such reviewer. Therefore, participation in engagement or making decisions for engagement team is to be avoided at all costs. However, engagement partner may consult engagement quality control reviewer during the engagement so as not to compromise his objectivity and eligibility to perform the role.

- ***Differences of Opinion:*** *There might be difference of opinion within engagement team, with those consulted and between engagement partner and engagement quality control reviewer. The report should only be issued after resolution of such differences. In case, recommendations of engagement quality control reviewer are not accepted by engagement partner and matter is not resolved to reviewer's satisfaction, the matter should be resolved by following established procedures of firm like by consulting with another practitioner or firm, or a professional or regulatory body.*

- ***Engagement documentation:*** *The firm should establish policies and procedures for engagement teams to complete the assembly of final engagement files on a timely basis after the engagement reports have been finalized. Engagement files should be completed in not more than 60 days after date of auditor's report in case of audit engagements and in other cases within the limits appropriate to engagements.*

Where two or more different reports are issued in respect of the same subject matter information of an entity, the firm's policies and procedures relating to time limits for the assembly of final engagement files should be considered for each report as if it were for a separate engagement.

Policies and procedures should be designed to maintain the confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation.

Care should be taken that policies and procedures on documentation of the engagement quality control review should require documentation that:-

(a) The procedures required by the firm's policies on engagement quality control review have been performed.

(b) The engagement quality control review has been completed before the report is issued and

(c) The reviewer is not aware of any unresolved matters that would cause the reviewer to believe that the significant judgments the engagement team made and the conclusions they reached were not appropriate.

Unless otherwise specified by law or regulation, engagement documentation is the property of the firm. The firm may, at its discretion, make portions of, or extracts from, engagement documentation available to clients, provided such disclosure does not undermine the validity of the work performed, or, in the case of assurance engagements, the independence of the firm or its personnel.

In the specific case of audit engagements, the retention period ordinarily is no shorter than seven years from the date of the auditor's report, or, if later, the date of the group auditor's report.

2.1.6. Monitoring

The firm should ensure that policies and procedures relating to the system of quality control are relevant, adequate, operating effectively and complied with in practice. Quality control of engagements has to be monitored taking into account following factors:

- Deciding whether quality control system of the firm has been appropriately designed and effectively implemented.
- Examining whether new developments in the professional standards, legal and regulatory requirements have been reflected in the quality control policies.
- Conducting monitoring by entrusting responsibility of monitoring process to a partner or other persons with sufficient and appropriate experience and authority in the firm.
- Dealing with complaints and allegations against the firm or any employees of it of non- compliance with professional standards or appropriate regulatory requirements.
- Taking appropriate remedial actions against the personnel who did not conform to quality control policies.

- Taking action when deficiencies in the design or operation of the firm's quality control policies and procedures, or non-compliance with the firm's system of quality control are identified.

3. SA-220 - QUALITY CONTROL FOR AN AUDIT OF FINANCIAL STATEMENTS:

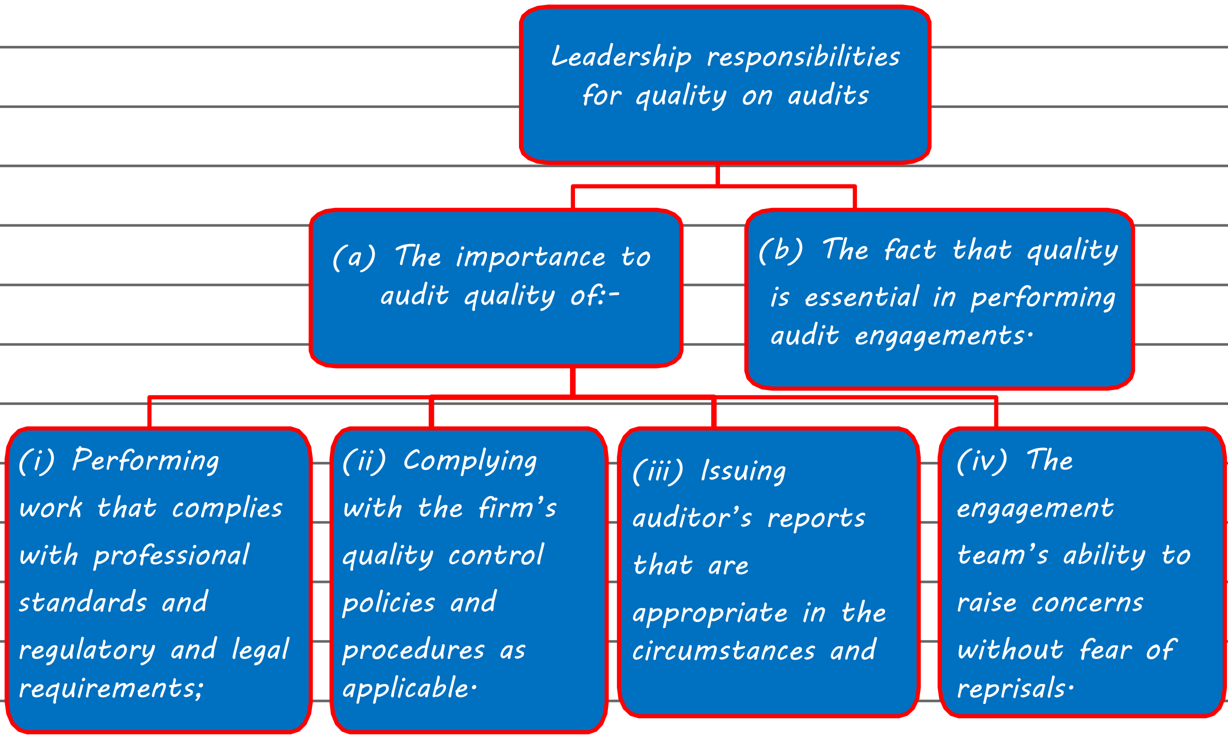
As per SA-220, the objective of the auditor is to implement quality control procedure the engagement level that Provide the auditor with reasonable assurance that:

(a) The audit complies with professional standards and regulatory and legal requirements and

(b) The auditor's report issued is appropriate in the circumstances.

SA-220 is modelled on lines of SQC 1.

3.1 Leadership Responsibilities for Quality on Audits



3.2 Relevant Ethical Requirements

The responsibilities of an engagement partner in relation to ethical requirements in an audit engagement are as under:-

- Identifying a threat to independence regarding the audit engagement that safeguards may not be able to eliminate or reduce to an acceptable level.
- Reporting by engagement partner to the relevant persons within the firm to determine

appropriate action, which may include eliminating the activity or interest that creates the threat, or withdrawing from the audit engagement, where withdrawal is legally permitted.

3.3 Acceptance and Continuance of Client Relationships and Audit Engagements

The responsibility of an engagement partner in this regard in an audit engagement is on lines of SQC 1.

3.4 Assignment of Engagement Teams

It should be ensured by engagement partner that the engagement team and any auditor's experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to perform the engagement in accordance with professional standards and regulatory and legal requirements.

3.5 Engagement Performance

Engagement partner has the responsibility for direction, supervision & performance of audit engagement in accordance with professional standards & regulatory & legal requirements.

3.6 Engagement Quality Control Review

For audits of financial statements of listed entities, and those other audit engagements, if any, for which the firm has determined that an engagement quality control review is required, the engagement partner shall:

(a) Determine that an engagement quality control reviewer has been appointed

(b) Discuss significant matters arising during the audit engagement, including those identified during the engagement quality control review, with the engagement quality control reviewer

(c) Not date the auditor's report until the completion of the engagement quality control review.

The engagement quality control reviewer shall perform an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor's report. This evaluation shall involve:

(a) Discussion of significant matters with the engagement partner

(b) Review of the financial statements and the proposed auditor's report

(c) Review of selected audit documentation relating to the significant judgments the engagement team made and the conclusions it reached and

(d) Evaluation of the conclusions reached in formulating the auditor's report and consideration of whether the proposed auditor's report is appropriate

For audits of financial statements of listed entities, the engagement quality control reviewer, on performing an engagement quality control review, shall also consider the following:

(a) The engagement team's evaluation of the firm's independence

(b) Whether appropriate consultation has taken place

(c) Whether audit documentation selected for review reflects the work performed in relation to the significant judgments made and supports the conclusions reached.

Differences of Opinion

If differences of opinion arise within the engagement team, with those consulted or, where applicable, between the engagement partner and the engagement quality control reviewer, the engagement team shall follow the firm's policies and procedures for dealing with and resolving differences of opinion.

3.7 Monitoring

The engagement partner shall consider the results of the firm's monitoring process as evidenced in the latest information circulated by the firm and, if applicable, other network firms & whether deficiencies noted in that information may affect the audit engagement.

3.8 Documentation

The engagement partner should document following matters pertaining to an audit engagement:-

- Issues identified with respect to compliance with relevant ethical requirements and how they were resolved.

- Conclusions on compliance with independence requirements that apply to the audit engagement, and any relevant discussions with the firm that support these conclusions.
- Conclusions reached regarding the acceptance and continuance of client relationships and audit engagements.
- The nature and scope of and conclusions resulting from, consultations undertaken during the course of the audit engagement.

4. SQC 1 VS. SA 220- KEY DIFFERENCES IN NATURE, SCOPE AND APPLICABILITY

S.N.	SQC 1	SA 220
1	It applies to entire firm and fixes the responsibility of firm to be assumed by CEO or managing partners.	It applies to a particular audit engagement and engagement partner takes responsibility of the same.
2	It is applicable to audits, reviews of historical financial Information, and other assurance and related services engagements.	It is applicable to audit engagements only.
3	It relates to setting up of a quality control system consisting of policies and procedures for firm as a whole.	It deals with responsibilities of engagement teams to implement quality control procedures that are applicable to audit engagements.
4	It pertains to establishing a system of quality control designed to provide firm with a reasonable assurance that a firm and its personnel comply with professional standards and regulatory and legal requirements so that reports issued by firm or engagement partners are appropriate in circumstances.	It is premised on the basis that firm is subject to SQC 1. Therefore, SQC 1 is a *sine qua non* for applicability of SA 220. It is within overall context of a firm's system of quality control, engagement teams implement quality control procedures applicable to audit engagements.

5. MECHANISMS FOR REVIEW OF QUALITY CONTROL

5.1 Peer Review Board

Peer review Board is constituted by Council of ICAI. The main objective of Peer review

Board is to ensure that, in carrying out assurance assignments: -

- Technical, professional and ethical standards including regulatory requirements are complied with by members of ICAI.
- Proper systems are in place including documentation thereof which amply demonstrate quality of assurance services provided by members.

The peer review is meant for purpose of enhancing quality of professional work resulting in more reliable and useful audit reports.

Peer review means an examination and review of the systems and procedures to determine whether the same have been put in place by the Practice Unit for ensuring the quality of assurance services as envisaged by the technical, professional and ethical Standards or any other regulatory requirements.

Once a Practice Unit is subjected to Peer review, its assurance engagement records pertaining to the Peer review period are subject to examination & review by the Peer Reviewer. On completion of this exercise, a "peer review certificate" is issued in case of unqualified report issued by Peer Reviewer. In case of a qualified report, it is informed to the Practice Unit that same cannot be issued along with the reasons therefor as well as inform about the due date for conducting a follow-on review as may be decided by the Board.

5.2 Quality Review Board

Quality review Board has been set up by Central government. It consists of members nominated by Central govt. and Council of ICAI. The functions of QRB are:-

(a) To make recommendations to the Council regarding the quality of services provided by the members of the Institute;

(b) To review the quality of services provided by the members of the Institute including audit services and

(c) To guide the members of the Institute to improve the quality of services and adherence to the various statutory and other regulatory requirements;

The statutory auditors in respect of the companies are identified for their audit quality review based upon risk-based approach. The review is carried out by technical reviewers who are empanelled by QRB on engagement basis from across the country.

5.3 National Financial Reporting Authority (NFRA)

NFRA has been constituted in terms of Section 132(1) of Companies Act, 2013.

Duties of NFRA also include the following: -

- Monitor and enforce compliance with accounting standards and auditing standards
- Oversee the quality of service of the professions associated with ensuring compliance with such standards and suggest measures for improvement in the quality of service.

It has power to monitor and enforce compliance with accounting standards and auditing standards and oversee the quality of service under section 132(2) or undertake investigation under section 132(4) of the auditors of certain class of companies. Such companies include listed companies, insurance companies, banking companies and other companies as provided for in rule 3 of NFRA Rules, 2018.

Therefore, overseeing quality of audit services of listed companies falls under the purview of NFRA. QRB can review quality of audit services provided by the members of the Institute only in respect of entities other than those specified under Rule 3 of NFRA Rules, 2018 and those referred to QRB by NFRA under relevant rules.

2. GENERAL AUDITING PRINCIPLES & AUDITORS RESPONSIBILITIES

1. GENERAL AUDITING PRINCIPLES AND AUDITOR'S RESPONSIBILITIES

SA 200 establishes the independent auditor's overall responsibilities when conducting an audit of financial statements in accordance with SAs. Audit has to be planned and performed with professional skepticism recognising that circumstances may exist that cause the financial statements to be materially misstated. Misstatements can arise from errors or frauds.

2. SA 240 "THE AUDITOR'S RESPONSIBILITIES RELATING TO FRAUD IN AN AUDIT OF FINANCIAL STATEMENTS"

2.1 The objectives of the auditor in accordance with SA 240 are: -

Objectives of the Auditor

- To identify and assess the risks of material misstatement in the financial statements due to fraud;
- To obtain sufficient appropriate audit evidence about the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and
- To respond appropriately to identified or suspected fraud.

❖ Meaning of Fraud and its Characteristics

Fraud is an intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.

Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the financial statements is intentional or unintentional.

Although fraud is a broad legal concept, the auditor is concerned with fraud that causes a material misstatement in the financial statements.

Fraud

- **Misstatements resulting from fraudulent financial reporting**
  - Involves incentive or pressure to commit fraud, a perceived opportunity and some rationalization of act
- **Misstatements resulting from misappropriation of assets**
  - Involves incentive or pressure to commit fraud, a perceived opportunity and some rationalization of act

2.2 How Fraudulent Financial Reporting may be caused by entities?

❖ **Fraudulent financial reporting may be accomplished by the following:**

- Manipulation, falsification (including forgery), or alteration of accounting records or supporting documentation from which the financial statements are prepared.
- Misrepresentation in or intentional omission from, the financial statements of events, transactions or other significant information.
- Intentional misapplication of accounting principles relating to amounts, classification, manner of presentation, or disclosure.

Fraudulent financial reporting often involves management override of controls that otherwise may appear to be operating effectively. Fraud can be committed by management overriding controls using such techniques as: -

- Recording fictitious journal entries, particularly close to the end of an account period, to manipulate operating results or achieve other objectives.
- Inappropriately adjusting assumptions and changing judgments used to estimate account balances.
- Omitting, advancing or delaying recognition in the financial statements of events and transactions that have occurred during the reporting period.
- Concealing, or not disclosing, facts that could affect the amounts recorded in financial statements.
- Engaging in complex transactions that are structured to misrepresent the financial position or financial performance of the entity.
- Altering records and terms related to significant and unusual transactions.

2.3 How misappropriation of assets may be accomplished by entities?

Misappropriation of assets can be accomplished in a variety of ways including:

- Embezzling receipts (for example, misappropriating collections on accounts receivable or diverting receipts in respect of written-off accounts to personal bank accounts).
- Stealing physical assets or intellectual property (for example, stealing inventory for personal use or for sale, stealing scrap for resale).
- Causing an entity to pay for goods and services not received (for example, payments to fictitious vendors, kickbacks paid by vendors).
- Using an entity's assets for personal use (for example, using the entity's assets as collateral for a personal loan or a loan to a related party).

Misappropriation of assets is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing or have been pledged without proper authorization.

2.4 Whose primary responsibility is to prevent and detect fraud?

The primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management.

2.5 Responsibilities of the Auditor

An auditor conducting an audit in accordance with SAs is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the SAs.

The potential effects of inherent limitations are particularly significant in the case of misstatement resulting from fraud. The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting one resulting from error. This is because fraud may involve sophisticated and carefully organized schemes designed to conceal it, such as forgery, deliberate failure to record transactions, or intentional misrepresentations being made to the auditor. Such attempts at concealment may be even more difficult to detect when accompanied by collusion. Collusion may cause the auditor to believe that audit evidence is persuasive when it is, in fact, false.

The auditor's ability to detect a fraud depends on factors such as the skillfulness of the perpetrator, the frequency & extent of manipulation, the degree of collusion involved, the relative size of individual amounts manipulated, & the seniority of those individuals involved.

Furthermore, the risk of the auditor not detecting a material misstatement resulting from management fraud is greater than for employee fraud, because management is frequently in a position to directly or indirectly manipulate accounting records, present fraudulent financial information or override control procedures designed to prevent similar frauds by other employees.

When obtaining reasonable assurance, the auditor is responsible for maintaining professional skepticism throughout the audit, considering the potential for management override of controls and recognizing the fact that audit procedures that are effective for detecting error may not be effective in detecting fraud.

What are fraud risk factors?

Fraud risk factors are events or conditions that indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud.

Examples of fraud risk factors: Following are examples of fraud risk factors relating to misstatements arising from fraudulent financial reporting and from misappropriation of assets respectively:-

[A] **Risk factors relating to misstatements arising from fraudulent financial reporting**

The following are examples of risk factors relating to misstatements arising from fraudulent financial reporting: -

Incentives/Pressures

Financial stability or profitability is threatened by economic, industry, or entity operating conditions, such as (or as indicated by):-

- *High degree of competition or market saturation, accompanied by declining margins.*
- *High vulnerability to rapid changes, such as changes in technology.*
- *Significant declines in customer demand and increasing business failures.*
- *Operating losses making the threat of bankruptcy, foreclosure, or hostile takeover.*
- *Recurring negative cash flows from operations.*
- *Rapid growth or unusual profitability especially compared to that of other companies.*
- *New Accounting Statutory or regulatory requirements.*

Excessive pressure exists for management to meet the requirements or expectations of third parties due to the following: -

- *Profitability or trend level expectations of investment analysts, institutional investors, significant creditors, or other external parties.*
- *Need to obtain additional debt or equity financing to stay competitive.*
- *Marginal ability to meet exchange listing requirements or debt repayment.*
- *Perceived or real adverse effects of reporting poor financial results on significant pending transactions, such as business combinations or contract awards.*

Information available indicates that the personal financial situation of management or those charged with governance is threatened by the entity's financial performance arising from the following:-

- *Significant financial interests in the entity.*
- *Significant portions of their compensation (for example, bonuses, stock options, and earn-out arrangements) being contingent upon achieving aggressive targets for stock price, operating results, financial position, or cash flow.*
- *Personal guarantees of debts of the entity.*
- *There is excessive pressure on management or operating personnel to meet financial targets.*

Opportunities: *The nature of the industry or the entity's operations provides opportunities to engage in fraudulent financial reporting that can arise from the following:*

- *Significant related-party transactions not in the ordinary course of business.*
- *A strong financial presence or ability to dominate a certain industry sector that allows the entity to dictate terms or conditions to suppliers or customers.*

- Assets, liabilities, revenues, or expenses based on significant estimates.
- Significant, unusual, or highly complex transactions.
- Significant operations located or conducted across international borders.
- Use of business intermediaries for which there appears to be no clear business justification.
- Significant bank accounts or subsidiary or branch operations in tax-haven jurisdictions.

The monitoring of management is not effective as a result of the following:

(i) Domination of management by a single person or small group (in a non owner-managed business) without compensating controls.

(ii) Oversight by those charged with governance over the financial reporting process and internal control is not effective.

There is a complex or unstable organizational structure, as evidenced by following: -

- Difficulty in determining the organization or individuals that have controlling interest in the entity.
- Overly complex organizational structure involving unusual legal entities or managerial lines of authority.
- High turnover of senior management, legal counsel, or those charged with governance

Internal control components are deficient as a result of the following: -

- Inadequate monitoring of controls, including automated controls and controls over interim financial reporting (where external reporting is required).
- High turnover rates or employment of accounting, internal audit, or information technology staff that are not effective.
- Accounting and information systems that are not effective, including situation involving significant deficiencies in internal control.

Attitudes/Rationalizations

- Communication, implementation, support, or enforcement of the entity's values or ethical standards by management, or the communication of inappropriate values or ethical standards, that are not effective.
- Non-financial management's excessive participation in or preoccupation with the selection

of accounting policies or the determination of significant estimates.

- Known history of violations of securities laws or other laws and regulations.
- Excessive interest by management in maintaining or increasing the entity's stock price or earnings trend.
- The practice by management of committing to analysts, creditors, and other third parties to achieve aggressive or unrealistic forecasts.
- Management failing to remedy known significant deficiencies in internal control.
- An interest by management in employing inappropriate means to minimize reported earnings for tax-motivated reasons.
- Low morale among senior management.
- The owner-manager makes no distinction between personal and business transactions.
- Dispute between shareholders in a closely held entity.
- Recurring attempts by management to justify marginal or inappropriate accounting.
- The relationship between management and the current or predecessor auditor is strained, as exhibited by the following: -
  - Frequent disputes with the current or predecessor auditor on accounting, auditing, or reporting matters.
  - Unreasonable demands on the auditor, such as unrealistic time constraints.
  - Restrictions on the auditor that inappropriately limit access to people or information.
  - Domineering management behaviour in dealing with the auditor.

[B] Risk factors relating to misstatements arising from misappropriation of assets

The following are examples of risk factors relating to misstatements arising from misappropriation of assets: -

Incentives/Pressures

Personal financial obligations may create pressure on management or employees with access to cash or other assets susceptible to theft to misappropriate those assets.

Adverse relationships between the entity and employees with access to cash or other assets susceptible to theft may motivate those employees to misappropriate those assets. For example, adverse relationships may be created by the following: -

- Known or anticipated future employee layoffs
- Recent or anticipated changes to employee compensation or benefit plans

- Promotions, compensation, or other rewards inconsistent with expectations

Opportunities

Certain characteristics or circumstances may increase the susceptibility of assets to misappropriation. For example, opportunities to misappropriate assets increase when there are the following: -

- *Large amounts of cash on hand*
- *Inventory items that are small in size, of high value, or in high demand.*
- *Easily convertible assets, such as bearer bonds, diamonds, or computer chips.*

Fixed assets which are small in size, marketable, or lacking observable identification of ownership.

Inadequate internal control over assets may increase the susceptibility of misappropriation those assets. For example, misappropriation of assets may occur because there is the following:

- *Inadequate segregation of duties or independent checks.*
- *Inadequate oversight of senior management expenditures.*
- *Inadequate management oversight of employees responsible for assets.*
- *Inadequate job applicant screening of employees with access to assets.*
- *Inadequate record keeping with respect to assets.*
- *Inadequate system of authorization and approval of transactions (for example purchasing).*
- *Inadequate physical safeguards over cash, investments, inventory, or fixed assets*
- *Lack of complete and timely reconciliations of assets.*
- *Lack of timely and appropriate documentation of transactions.*
- *Lack of mandatory vacations for employees performing key control functions.*
- *Inadequate management understanding of information technology.*
- *Inadequate access controls over automated records.*

Attitudes/Rationalizations

- *Disregard for the need for monitoring or reducing risks related to misappropriations of assets.*
- *Disregard for internal control over misappropriation of assets.*
- *Behaviour indicating displeasure or dissatisfaction with the entity.*

- Changes in behaviour or lifestyle that may indicate assets have been misappropriated.
- Tolerance of petty theft.

Why evaluation of fraud risk factors by auditor is necessary?

The auditor shall evaluate whether one or more fraud risk factors are present. While fraud risk factors may not necessarily indicate the existence of fraud, they have often been present in circumstances where frauds have occurred and therefore may indicate risks of material misstatement due to fraud.

2.6 Maintaining Professional Skepticism

The auditor shall maintain professional skepticism throughout the audit, recognizing the possibility that a material misstatement due to fraud could exist, notwithstanding the auditor's past experience of the honesty and integrity of the entity's management and those charged with governance.

2.7 Discussion among the engagement team

The discussion among the engagement team shall place particular emphasis on how and where the entity's financial statements may be susceptible to material misstatement due to fraud, including how fraud might occur.

2.8. Risk assessment procedures and related activities be geared towards obtaining information for use in identifying risk of material misstatement due to fraud

When performing risk assessment procedures and related activities to obtain an understanding of the entity and its environment, including the entity's internal control, the auditor shall perform the procedures to obtain information for use in identifying the risks of material misstatement due to fraud like inquiries of management and others within the entity, obtaining understanding as to how those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control that management has established to mitigate these risks and evaluation of unexpected relationships identified in performing analytical procedures which may indicate risks of material misstatement due to fraud.

2.9 Responses to the assessed risks of material misstatement due to fraud at the financial statement level

In determining overall responses to address the assessed risks of material misstatement due to fraud at the financial statement level, the auditor shall:-

(a) Assign and supervise personnel taking account of the knowledge, skill and ability of the individuals to be given significant engagement responsibilities and the auditor's assessment of the risks of material misstatement due to fraud for the engagement;

(b) Evaluate whether the selection & application of accounting policies by the entity, particularly those related to subjective measurements & complex transactions, may be indicative of fraudulent financial reporting resulting from management's effort to manage earnings; and

(c) Incorporate an element of unpredictability in the selection of the nature, timing and extent of audit procedures.

2.10 Audit procedures responsive to assessed risks of material misstatement due to fraud at the assertion level

The auditor shall design and perform further audit procedures whose nature, timing and extent are responsive to the assessed risks of material misstatement due to fraud at the assertion level. In doing so, the auditor may change nature, timing and extent of audit procedures to obtain audit evidence that is more reliable and relevant or to obtain additional corroborative information.

2.11 Audit procedures responsive to risks related to management override of controls

Management is in a unique position to perpetrate fraud because of management's ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. This risk is present in all entities. Due to the unpredictable way in which such override could occur, it is a risk of material misstatement due to fraud and thus a significant risk.

Irrespective of the auditor's assessment of the risks of management override of controls, the auditor shall design and perform audit procedures to:-

(a) Test the appropriateness of journal entries recorded in the general ledger.

(b) Review accounting estimates for biases.

(c) For significant transactions that are outside the normal course of business for the entity or that otherwise appear to be unusual given the auditor's understanding of the entity and its environment and other information obtained during the audit, the auditor shall evaluate whether the business rationale (or the lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets.

2.12 Evaluation of Audit Evidence

The auditor shall evaluate whether analytical procedures that are performed when forming an overall conclusion as to whether the financial statements as a whole are consistent with the auditor's understanding of the entity and its environment.

When the auditor identifies a misstatement, the auditor shall evaluate whether such a misstatement is indicative of fraud.

If the auditor identifies a misstatement, whether material or not, and the auditor has reason to believe that it is or may be the result of fraud and that management (in particular, senior management) is involved, the auditor shall re- evaluate the assessment of the risks of material misstatement due to fraud and its resulting impact on the nature, timing and extent of audit procedures to respond to the assessed risks.

When the auditor confirms that, or is unable to conclude whether, the financial statements are materially misstated as a result of fraud, the auditor shall evaluate the implications for the audit.

2.13 Circumstances in which auditor is unable to continue the engagement

Auditor is unable to continue the Engagement

(a) Determine the professional and legal responsibilities applicable in the circumstances.

(b) Consider whether it is appropriate to withdraw from the engagement, where withdrawal from the engagement is legally permitted; and

(c) If the auditor withdraws

(i) Discuss with the appropriate level of management and those charged with governance

(ii) Determine whether there is a professional or legal requirement to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities.

2.14 Management Representations

The auditor shall obtain written representations from management and, where applicable, those charged with governance that: -

(a) They acknowledge their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud;

(b) They have disclosed to the auditor the results of management's assessment of the risk that the financial statements may be materially misstated as a result of fraud;

(c) They have disclosed to the auditor their knowledge of fraud or suspected fraud and

(d) They have disclosed to the auditor their knowledge of any allegations of fraud, or suspected fraud.

2.15 Communications to Management and with Those Charged With Governance

If the auditor has identified a fraud or has obtained information that indicates that a fraud may exist, the auditor shall communicate these matters on a timely basis to the appropriate level of management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities.

If the auditor suspects fraud involving management, the auditor shall communicate these suspicions to those charged with governance and discuss with them the nature, timing and extent of audit procedures necessary to complete the audit.

The auditor shall communicate with those charged with governance any other matters related to fraud that are, in the auditor's judgment, relevant to their responsibilities.

2.16 Communications to Regulatory and Enforcement Authorities

If the auditor has identified or suspects a fraud, the auditor shall determine whether there is a responsibility to report the occurrence or suspicion to a party outside the entity.

3. SA 250 "CONSIDERATION OF LAWS AND REGULATIONS IN AN AUDIT OF FINANCIAL STATEMENTS"

3.1 Effect of Laws and Regulations on Financial Statements of an Entity

The provisions of some laws or regulations have a direct effect on the financial statements in that they determine the reported amounts and disclosures in an entity's financial statements. Other laws or regulations are to be complied with by management or set the provisions under which the entity is allowed to conduct its business but do not have a direct effect on an entity's financial statements.

3.2 Objectives of auditor in accordance with SA 250

(a) To obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements;

(b) To perform specified audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements; and

(c) To respond appropriately to non-compliance or suspected non-compliance with laws and regulations identified during the audit.

3.3 Responsibility of Management for Compliance with Laws and Regulations

The following are examples of the types of policies and procedures an entity may implement to assist in the prevention and detection of non-compliance with laws and regulations: -

- Monitoring legal requirements and ensuring that operating procedures are design meet these requirements.
- Instituting and operating appropriate systems of internal control.
- Developing, publicising and following a code of conduct.
- Ensuring employees are properly trained and understand the code of conduct.
- Monitoring compliance with the code of conduct and acting appropriately to discipline employees who fail to comply with it.
- Engaging legal advisors to assist in monitoring legal requirements.
- Maintaining a register of significant laws and regulations with which the entity has comply within its particular industry and a record of complaints.

In larger entities, these policies and procedures may be supplemented by assigning appropriate responsibilities to an internal audit function, an audit committee, a compliance function.

3.4 Responsibility of the Auditor

The auditor is not responsible for preventing non-compliance and cannot be expected to detect non- compliance with all laws and regulations. The auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, whether caused by fraud or error.

In the context of laws and regulations, the potential effects of inherent limitations on the auditor's ability to detect material misstatements are greater for such reasons as the following:-

- There are many laws and regulations, relating principally to the operating aspects of an entity that typically do not affect the financial statements and are not captured by the entity's information systems relevant to financial reporting.
- Non-compliance may involve conduct designed to conceal it, such as collusion, forgery, deliberate failure to record transactions, management override of controls or intentional misrepresentations being made to the auditor.
- Whether an act constitutes non-compliance is ultimately a matter for legal determination by a court of law.

SA 250 distinguishes the auditor's responsibilities in relation to compliance with two different categories of laws and regulations as follows:-

For the compliance with provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements, the auditor's responsibility is to obtain sufficient appropriate audit evidence about compliance with the provisions of those laws and regulations.

For other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements but compliance with which may be fundamental to the operating aspects of the business, the auditor's responsibility is limited to undertaking specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial statements.

The Auditor's consideration of compliance with laws and regulations

(1) As part of obtaining an understanding of the entity and its environment, the auditor shall obtain a general understanding of:-

(a) The legal and regulatory framework applicable to the entity and the industry or sector in which the entity operates; and

(b) How the entity is complying with that framework

(2) The auditor shall perform the following audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements:

(a) Inquiring of management and, where appropriate, those charged with governance, whether the entity is incompliance with such laws and regulations; and

(b) Inspecting correspondence, if any, with the relevant licensing or regulatory authorities.

(3) Certain other laws and regulations may need particular attention by the auditor because they have a fundamental effect on the operations of the entity. Non-compliance with laws and regulations that have a fundamental effect on the operations of the entity may cause the entity to cease operations, or call into question the entity's continuance as a going concern.

(4) Audit procedures applied to form an opinion on the financial statements may bring instances of non- compliance or suspected non-compliance with laws and regulations to the auditor's attention.

(5) During the audit, the auditor shall remain alert to the possibility that other audit procedures applied may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention.

(6) The auditor shall request management and, where appropriate, those charged with governance to provide written representations that all known instances of non-compliance or suspected non- compliance with laws and regulations whose effects should be considered when preparing financial statements have been disclosed to the auditor.

3.5	**Audit Procedures when Non-Compliance is Identified or Suspected**
(1)	**If the auditor becomes aware of information concerning an instance of non-compliance or suspected non-compliance with laws and regulations, the auditor shall obtain:**
(a)	**An understanding of the nature of the act & the circumstances in which it has occurred and**
(b)	**Further information to evaluate the possible effect on the financial statements.**
(2)	If the auditor suspects there may be non-compliance, the auditor shall discuss the matter with management and, where appropriate, those charged with governance. If management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, in the auditor's judgment, the effect of the suspected non-compliance may be material to the financial statements, the auditor shall consider the need to obtain legal advice.
(3)	If sufficient information about suspected non-compliance cannot be obtained, the auditor shall evaluate the effect of the lack of sufficient appropriate audit evidence on the auditor's opinion.
(4)	The auditor shall evaluate the implications of non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations, and take appropriate action.
3.6	**Reporting of Identified or Suspected Non-Compliance**
(A)	**Reporting Non-Compliance to Those Charged with Governance**
(1)	The auditor shall communicate with those charged with governance matters involving non- compliance with laws and regulations that come to the auditor's attention during the course of the audit, other than when the matters are clearly inconsequential.
(2)	If, in the auditor's judgment, the non-compliance referred to above is believed to be intentional and material, the auditor shall communicate the matter to those charged with governance as soon as practicable.
(3)	If the auditor suspects that management or those charged with governance are involved in non- compliance, the auditor shall communicate the matter to the next higher level of authority at the entity, if it exists, such as an audit committee or supervisory board. Where no higher authority exists, or if the auditor believes that the communication may not be acted upon or is unsure as to the person to whom to report, the auditor shall consider the need to obtain legal advice.

(B) **Reporting non-compliance in the auditor's report on the financial statements**

(1) If the auditor concludes that the non-compliance has a material effect on the financial statements, and has not been adequately reflected in the financial statements, the auditor shall, in accordance with SA 705, express a qualified or adverse opinion on the financial statements.

(2) If the auditor is precluded by management or those charged with governance from obtaining sufficient appropriate audit evidence to evaluate whether non-compliance that may be material to the financial statements has, or is likely to have, occurred, the auditor shall express a qualified opinion or disclaim an opinion on the financial statements on the basis of a limitation on the scope of the audit in accordance with SA 705.

(3) If the auditor is unable to determine whether non-compliance has occurred because of limitations imposed by the circumstances rather than by management or those charged with governance, the auditor shall evaluate the effect on the auditor's opinion in accordance with SA 705.

(C) **Reporting non-compliance to regulatory and enforcement authorities**

If the auditor has identified or suspects non-compliance with laws and regulations, the auditor shall determine whether the auditor has a responsibility to report the identified or suspected non- compliance to parties outside the entity.

4. SA 260 "COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE"

SA 260 deals with the auditor's responsibility to communicate with those charged with governance in an audit of financial statements

Who are "Those charged with governance"?

"Those charged with governance" denote the person(s) or organization(s) (e.g., a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes those overseeing the financial reporting process. For some entities, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

Governance structures vary by entities, reflecting influences such as different cultural and legal backgrounds, size and ownership characteristics. For example, in some entities, a supervisory board exists that is separate from executive board. In other entities, both supervisory and executive functions are performed by a single board. In some entities, those charged with governance hold positions that are an integral part of the entity's legal structure. For example, company directors. In some cases, some or all of those charged with governance are involved in managing the entity. In others, those charged with governance and management comprise different persons.

4.1 Objectives of Auditor in Accordance with SA 260

The objectives of the auditor are:-

(a) To communicate clearly with those charged with governance responsibilities of the auditor in relation to the financial statement audit, and an overview of the planned scope and timing of the audit;

(b) To obtain from those charged with governance information relevant to the audit;

(c) To provide those charged with governance with timely observations arising from the audit that are significant and relevant to their responsibility to oversee the financial reporting process; and

(d) To promote effective two-way communication between the auditor and those charged with governance.

4.2 Matters to be communicated by the Auditor

Following matters are required to be communicated by auditor with those charged with governance:-

(a) The auditor's responsibilities in relation to the financial statement audit

- The auditor is responsible for forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance and
- The audit of the financial statements does not relieve management or those charged governance of their responsibilities.

(b) Planned scope and timing of the audit

Communication regarding the planned scope and timing of the audit may: -

- Assist those charged with governance to understand better the consequences of the auditor's work, to discuss issues of risk and the concept of materiality with the auditor, and to identify any areas in which they may request the auditor to undertake additional procedures and
- Assist the auditor to understand better the entity and its environment.

(c) Significant findings from the audit

The auditor shall communicate with those charged with governance:-

(i) The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures.

(ii) Significant difficulties, if any, encountered during the audit

(iii) Unless all of those charged with governance are involved in managing the entity:

(1) Significant matters arising during the audit that were discussed, or subject to correspondence, with management;

(2) Written representations the auditor is requesting

(iv) Circumstances that affect the form and content of the auditor's report, if any and

(v) Any other significant matters arising during the audit that, in the auditor's professional judgment, are relevant to the oversight of the financial reporting process.

The communication of findings from the audit may include requesting further information from those charged with governance in order to complete the audit evidence obtained. For example, the auditor may confirm that those charged with governance have the same understanding of the facts and circumstances relevant to specific transactions or events.

❖ **Significant difficulties encountered during the audit may include such matters as:-**

- Significant delays by management, the unavailability of entity personnel, or an unwillingness by management to provide information necessary for the auditor to perform the auditor's procedures.
- An unreasonably brief time within which to complete the audit.
- Extensive unexpected effort required to obtain sufficient appropriate audit evidence.
- The unavailability of expected information.

- Restrictions imposed on the auditor by management.
- Management's unwillingness to make or extend its assessment of the entity's ability to continue as a going concern when requested.

In some circumstances, such difficulties may constitute a scope limitation that leads to a modification of the auditor's opinion.

Significant matters that were discussed, or subject to correspondence with management include such matters as:-

- Significant events or transactions that occurred during the year.
- Business conditions affecting the entity, and business plans and strategies that may affect the risks of material misstatement.
- Concerns about management's consultations with other accountants on accounting or auditing matters.
- Discussions or correspondence in connection with the initial or recurring appointment of the auditor regarding accounting practices, the application of auditing standards, or fees for audit or other services.
- Significant matters on which there was disagreement with management, except initial differences of opinion because of incomplete facts or preliminary information that are later resolved by the auditor obtaining additional relevant facts or information.

Circumstances in which the auditor is required or may otherwise consider it necessary to include additional information in the auditor's report in accordance with the SAs, and for which communication with those charged with governance is required, include when:

- The auditor expects to modify the opinion in the auditor's report in accordance with SA 705.
- A material uncertainty related to going concern is reported in accordance with SA 570.
- Key audit matters are communicated in accordance with SA 701.
- The auditor considers it necessary to include an Emphasis of Matter paragraph or Other Matter paragraph in accordance with SA 706 or is required to do so by other SAs.
- The auditor has concluded that there is an uncorrected material misstatement of the other information in accordance with SA 720.

4.3 Communication of Auditor's Independence in Case of Listed Entities

In the case of listed entities, the auditor shall communicate with those charged with governance: -

(a) A statement that the engagement team and others in the firm as appropriate, the firm and, when applicable, network firms have complied with relevant ethical requirements regarding independence; and

(b)

i. All relationships and other matters between the firm, network firms, and the entity that, in the auditor's professional judgment, may reasonably be thought to bear on independence. This shall include total fees charged during the period covered by the financial statements for audit and non-audit services provided by the firm and network firms to the entity and components controlled by the entity. These fees shall be allocated to categories that are appropriate to assist those charged with governance in assessing the effect of services on the independence of the auditor; and

ii. The related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level.

The Communication process

The auditor shall communicate with those charged with governance the form, timing and expected general content of communications.

The auditor shall communicate in writing with those charged with governance regarding significant findings from the audit if, in the auditor's professional judgment, oral communication would not be adequate. Written communications need not include all matters that arose during the course of the audit. The auditor shall communicate in writing with those charged with governance regarding auditor independence when required in case of listed entities.

The auditor shall communicate with those charged with governance on a timely basis.

Adequacy of the communication process

The auditor shall evaluate whether the two-way communication between the auditor and those charged with governance has been adequate for the purpose of the audit.

If it has not, the auditor shall evaluate the effect, if any, on the auditor's assessment of the risks of material misstatement and ability to obtain sufficient appropriate audit evidence, and shall take appropriate action.

5. SA 299 "JOINT AUDIT OF FINANCIAL STATEMENTS"

5.1 Objectives in accordance with SA 299

The objectives in accordance with SA 299 are as under:-

(a) To lay down broad principles for the joint auditors in conducting the joint audit.

(b) To provide a uniform approach to the process of joint audit.

(c) To identify the distinct areas of work and coverage thereof by each joint auditor.

(d) To identify individual responsibility and joint responsibility of the joint auditors in relation to audit.

5.2. Audit planning, Risk Assessment and Allocation of Work

(1) Prior to the commencement of the audit, the joint auditors shall discuss and develop a joint audit plan. In developing the joint audit plan, the joint auditors shall:

(a) Identify division of audit areas and common audit areas amongst the joint auditors that define the scope of the work of each joint auditor. Where joint auditors are appointed, should, by mutual discussion, divide the audit work among themselves. The division work would usually be in terms of audit of identifiable units or specified areas. In some cases, due to the nature of the business of the entity under audit, such a division of work may not be possible. In such situations, the division of work may be with reference to items of assets or liabilities or income or expenditure.

(b) Ascertain the reporting objectives of the engagement to plan the timing of the audit the nature of the communications required

(c) Consider and communicate among all joint auditors the factors that, in their professional judgment, are significant in directing the engagement team's efforts

(d) Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other or similar engagements performed earlier by respective engagement partner for the entity is relevant.

(e) Ascertain the nature, timing and extent of resources necessary to perform engagement.

(2) ***At this stage, risks of material misstatement need to be considered*** *and assessed by each of the joint auditors and shall be communicated to other joint auditors, and documented, whether pertaining to the overall financial statements level or to the area of allocation among the other joint auditors.*

(3) ***The joint auditors shall discuss and document the nature, timing, and the extent of the audit procedures*** *for common and specific allotted areas of audit to be performed by each of the joint auditors and the same shall be communicated to those charged with governance.*

(4) ***The joint auditors shall obtain common engagement letter*** *and common management representation letter.*

(5) ***After identification and allocation of work among the joint auditors, the work allocation document shall be signed by all the joint auditors*** *and the same shall be communicated to those charged with governance of the entity.*

5.3 Responsibility and Co-ordination among Joint Auditors

In respect of audit work dividend among the joint auditor such *joint auditor shall be responsible only for the work allocated to such joint auditor including proper execution of the audit procedures. In cases where specific divisions, zones or units are allocated to different joint auditors, it is the separate and specific responsibility of each joint auditor to obtain information and explanations from the management in respect of such divisions/zones/units and to evaluate the information and explanations so obtained by said joint auditor. The joint auditors shall have proper coordination and rationality wherever required.*

All the joint auditors shall be jointly and severally responsible for:-

(a) *the audit work which is not divided among the joint auditors and is carried out by all joint auditors*

(b) *decisions taken by all the joint auditors under audit planning in respect of common audit areas concerning the nature, timing and extent of the audit procedures to be performed by each of the joint auditors.*

(c) matters which are brought to the notice of the joint auditors by any one of them and on which the is an agreement among the joint auditors

(d) examining that the financial statements of the entity comply with the requirements of the relevant statutes

(e) presentation and disclosure of the financial statements as required by the applicable financial reporting framework

(f) ensuring that the audit report complies with the requirements of the relevant statutes, the applicable Standards on Auditing and the other relevant pronouncements issued by ICAI.

Where, in the course of the audit, a joint auditor comes across matters which are relevant to the areas of responsibility of other joint auditors and which deserve their attention, require disclosure or require discussion with, or application of judgment by other joint auditors, the said joint auditor shall communicate the same to all the other joint auditors in writing prior to the completion of the audit.

It shall be the responsibility of each joint auditor to determine the nature, timing and extent of audit procedures to be applied in relation to the areas of work allocated to said joint auditor. It is the individual responsibility of each joint auditor to study and evaluate the prevailing system of internal control and assessment of risk relating to the areas of work allocated to said joint auditor.

As regards decisions taken by all the joint auditors under audit planning in respect of common audit areas concerning the nature, timing and extent of the audit procedures to be performed by each of the joint auditors, all the joint auditors are responsible only in respect of the appropriateness of the decisions concerning the nature, timing and extent of the audit procedures agreed upon among them, proper execution of these audit procedures is the individual responsibility of the joint auditor concerned.

5.4 Audit Conclusion and Reporting

The joint auditors are required to issue common audit report, however, where the joint auditors are in disagreement with regard to the opinion or any matters to be covered by the audit report, they shall express their opinion in a separate audit report. A joint auditor is not bound by the views of the majority of the joint auditors regarding the opinion or matters to be covered in the audit report and shall express opinion formed by the said joint auditor in separate audit report in case of disagreement. In such circumstances, the audit report(s) issued by the joint auditor(s) shall make a reference to the separate audit report(s) issued by the other joint auditor(s). Further, separate audit report shall also make reference to the audit report issued by other joint auditors. Such reference shall be made under the heading "Other Matter Paragraph" as per SA 706.

Each Joint Auditor is entitled to assume that:

(a) It is not necessary for a joint auditor to review the work performed by other joint auditors or perform any tests in order to ascertain whether the work has actually been performed in such a manner.

(b) The other joint auditors have brought to said joint auditor's notice any departure from applicable financial reporting framework or significant observations that are relevant to their responsibilities noticed in the course of the audit.

6. SA 402 "AUDIT CONSIDERATIONS RELATING TO AN ENTITY USING A SERVICE ORGANISATION"

What is a Service organization?

- Service organisation is a third-party organisation (or segment of a third-party organisation) that provides services to user entities that are part of those entities' information systems relevant to financial reporting. User entity is an entity that uses a service organisation and whose financial statements are being audited.

Who is a service auditor?

- Service auditor is an auditor who, at the request of the service organisation, provides an assurance report on the controls of a service organisation. User auditor is an auditor who audits and reports on the financial statements of a user entity.

6.1 Objectives of user auditor in accordance with SA 402

Objectives of the auditor

- To obtain an understanding of the nature and significance of the services provided by the service organisation and their effect on the user entity's internal control relevant to the audit, sufficient to identify and assess the risks of material misstatement; and
- To design and perform audit procedures responsive to those risks.

6.2 Type 1 report and Type 2 report

❖ **Refer Paragraph 3.3 of Chapter 2**

6.3 Obtaining an Understanding of the Services

1. **Obtaining an understanding of the services provided by a service organisation, including internal control:**

(a) The nature of the services provided by the service organisation and the significance of those services to the user entity, including the effect thereof on the user entity's internal control.

(b) The nature and materiality of the transactions processed or accounts or financial reporting processes affected by the service organisation.

(c) The degree of interaction between the activities of the service organisation and those of the user entity. The degree of interaction refers to the extent to which a user entity is able to and elects to implement effective controls over the processing performed by the service organisation.

(d) The nature of the relationship between the user entity and the service organisation, including the relevant contractual terms for the activities undertaken by the service organisation.

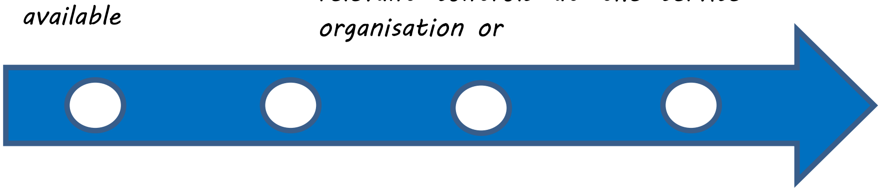
2. **When obtaining an understanding of internal control relevant to the audit in accordance with SA 315, the user auditor shall evaluate the design and implementation of relevant controls** at the user entity that relate to the services provided by the service organisation, including those that are applied to the transactions processed by the service organisation.

3. ***The user auditor shall determine whether a sufficient understanding of the nature and significance of the services*** *provided by the service organisation and their effect on the user entity's internal control relevant to the audit has been obtained to provide a basis for the identification and assessment of risks of material misstatement.*

4. ***If the user auditor is unable to obtain a sufficient understanding from the user entity, the user auditor shall obtain that understanding from one or more of the following procedures:-***

(a) Obtaining a Type 1 or Type 2 report, if available

(c) Visiting the service organisation and performing procedures that will provide the necessary information about the relevant controls at the service organisation or



(b) Contacting the service organisation, through the user entity, to obtain specific information

(d) Using another auditor to perform procedures that will provide the necessary information about the relevant controls at the service organisation.

6.4 *Using Type 1or Type 2 Report*

Using A Type 1 Or Type 2 Report to Support the User Auditor's Understanding of The Service Organisation: In determining the sufficiency and appropriateness of the audit evidence provided by a Type 1 or Type 2 report, the user auditor shall be satisfied as to: -

(a) *The service auditor's professional competence (except where the service auditor is a member of the Institute of Chartered Accountants of India) and independence from the service organisation; and*

(b) *The adequacy of the standards under which the Type 1 or Type 2 report was issued.*

If the user auditor plans to use a Type 1 or Type 2 report as audit evidence to support the user auditor's understanding about the design and implementation of controls at the service organisation, the user auditor shall:

(a) Evaluate whether the description and design of controls at the service organisation is at a date or for a period that is appropriate for the user auditor's purposes;

(b) Evaluate the sufficiency and appropriateness of the evidence provided by the report and

(c) Determine whether complementary user entity controls identified by service organisation are relevant to the user entity.

Complementary user entity controls refer to controls that the service organisation assumes, in the design of its service, will be implemented by user entities, and which, if necessary to achieve control objectives, are identified in the description of its system.

6.5 Responding to the Assessed Risks of Material Misstatement

In responding to assessed risks in accordance with SA 330, the user auditor shall: -

(a) Determine whether sufficient appropriate audit evidence concerning the relevant financial statement assertions is available from records held at the user entity; and, if not,

(b) Perform further audit procedures to obtain sufficient appropriate audit evidence or use another auditor to perform those procedures at the service organisation on the user auditor's behalf.

6.6 Tests of Controls

When the user auditor's risk assessment includes an expectation that controls at the service organisation are operating effectively, the user auditor shall obtain audit evidence about the operating effectiveness of those controls from one or more of the following procedures: -

(a) Obtaining a Type 2 report, if available;

(b) Performing appropriate tests of controls at the service organisation; or

(c) Using another auditor to perform tests of controls at the service organisation on behalf of the user auditor.

If, the user auditor plans to use a Type 2 report as audit evidence that controls at the service organisation are operating effectively, the user auditor shall determine whether the service auditor's report provides sufficient appropriate audit evidence about the effectiveness of the controls to support the user auditor's risk assessment by:

(a) Evaluating whether the description, design and operating effectiveness of controls at the service organisation is at a date or for a period that is appropriate for the user auditor's purposes;

(b) Determining whether complementary user entity controls identified by the service organisation are relevant to the user entity

(c) Evaluating the adequacy of the time period covered by the tests of controls.

(d) Evaluating whether the tests of controls performed by the service auditor and the results thereof, as described in the service auditor's report, are relevant to the assertions.

6.7 Fraud, non-compliance with laws and regulations and uncorrected misstatements in relation to activities at the service organisation

The user auditor shall evaluate how such matters affect the nature, timing and extent of the user auditor's further audit procedures, including the effect on the user auditor's conclusions and user auditor's report.

6.8 Reporting by the user auditor

The user auditor shall modify the opinion in the user auditor's report in accordance with SA 705 if the user auditor is unable to obtain sufficient appropriate audit evidence regarding the services provided by the service organisation relevant to the audit of the user entity's financial statements.

3. AUDIT PLANNING, STRATEGY & EXECUTION

1. COMMENCING AN AUDIT

SA 200 "Overall Objectives of the Independent Auditor and the Conduct of an Audit in accordance with Standards on Auditing" states that in order to achieve the overall objectives of the audit, the auditor shall use the objectives stated in relevant SAs in planning and performing the audit. Without a careful plan, the overall objective of an audit may not be achieved. The audit planning is necessary to conduct an effective audit, in an efficient and timely manner.

1.1 Benefits/Advantages of Planning in an Audit of Financial Statements

(i) Attention to Important areas

(ii) Timely resolution of Potential Problems

(iii) Proper Organisation and Management of Audit Engagement.

(iv) Proper Selection of Engagement Team

(v) Direction and Supervision of Engagement Team

(vi) Easy Coordination in work done by auditors of components and experts.

1.2 Nature and Extent of Planning

So far as the nature of planning is concerned, it would vary according to-

(i) **Size and Complexity of the Auditee -** If the size and complexity of organization of which audit is to be conducted is large, then much more planning activities would be required as compared to an entity whose size and complexity is small.

(ii) **Past Experience & Expertise -** The key engagement team members' previous experience & expertise also contributes towards variation in planning activities.

(iii) **Change in Circumstances -** Another factor contributing towards variation in planning activities is change in circumstances.

1.3 Planning - A Continuous Process

Planning is not a discrete phase of an audit but rather a continual and iterative process. It often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement.

Planning includes consideration of the timing of certain activities and audit procedures. It also involves Audit Programming.

1. **Planning includes the need to consider such matters as:**

- The analytical procedures to be applied as risk assessment procedures.
- Obtaining a general understanding of the legal and regulatory framework applicable to the entity and how the entity is complying with that framework.
- The determination of materiality.
- The involvement of experts.
- The performance of other risk assessment procedures.

1.4 Overall Audit Strategy and Audit Plan - Responsibility of the Auditor

The auditor may decide to discuss elements of planning with the entity's management to facilitate the conduct and management of the audit engagement.

Although these discussions often occur but the overall audit strategy and the audit plan remain the auditor's responsibility. When discussing matters about the overall audit strategy or audit plan, care is required in order not to compromise the effectiveness of the audit to be taken to see there is no compromise in the effectiveness of the audit.

The engagement partner and other key members of the engagement team should be involved in planning the audit.

1.5 Acceptance and Continuance of Client Relationships and Audit Engagements

Acceptance and Continuance of Client Relationships and Audit Engagements are very important preliminary engagement activities.

The auditor shall undertake the following activities at the beginning of the current audit engagement-

(i) Performing procedures required by SA 220, "Quality Control for an Audit of Financial Statements" regarding the continuance of the client relationship and the specific audit engagement.

(ii) Evaluating compliance with ethical requirements, including independence, as required by SA 220; and

(iii) Establishing an understanding of the terms of the engagement, as required by SA 210.

1.6 Contents of an Audit Plan

The auditor should develop an audit plan that shall include a description of-

(i) The nature, timing and extent of planned risk assessment procedures, as determined under SA 315 "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment".

(ii) The nature, timing and extent of planned further audit procedures at the assertion level, as determined under SA 330 "The Auditor's Responses to Assessed Risks".

(iii) Other planned audit procedures that are required to be carried out so that the engagement complies with SAs.

1.7 Changes to Planning Decisions

The auditor may need to modify the overall audit strategy and audit plan due to below mentioned factors-

(i) Result of Unexpected events,

(ii) Changes in conditions, or

(iii) The audit evidence obtained from the results of audit procedures.

Further, the auditor would also have to modify the nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks.

This may be the case when information coming to the auditor differs significantly from the information when he planned the audit procedures.

In addition to above, there may be a possibility of change in law, notifications, Govt. policies which warrants updating of overall Audit strategy.

2. OVERALL AUDIT STRATEGY

The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan.

2.1 Factors while establishing Overall Audit Strategy

Overall audit strategy would involve-

(i) **Determination of Characteristics of Audit:** Identify the characteristics of the engagement that defines its scope.

(ii) **Reporting Objectives:** Ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required.

(iii) **Team's Efforts:** Consider the factors that, in the auditor's professional judgment, are significant in directing the engagement team's efforts.

(iv) **Considering result of preliminary engagement activities:** Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed by the engagement partner for the entity is relevant.

(v) **Nature, timing and Extent of Resources:** Ascertain the nature, timing and extent of resources necessary to perform the engagement.

2.2 Benefits of Overall Audit Strategy

The process of establishing the overall audit strategy assists the auditor to determine such matters as-

(i) **Employment of Qualitative Resources:** The resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas or the involvement of experts on complex matters like review of valuation, hedging transactions.

(ii) **Allocation of Quantity of Resources:** The amount of resources to allocate to specific audit areas, such as the number of team members assigned to observe the inventory count at material locations, the extent of review of other auditors' work in the case of group audits, or the allocation of audit budgeted hours to high risk areas.

(iii) **Timing of Deployment of Resources:** When these resources are to be deployed, such as whether at an interim audit stage or at or close to key cut-off dates.

(iv) **Management of Resources:** How such resources shall be managed, directed & supervised, etc.,

2.3 Considerations in Establishing the Overall Audit Strategy

Some of the examples of matters that the auditor may consider in establishing the overall audit strategy are given hereunder. Many of these matters will also influence the auditor's detailed audit plan. All matters are not relevant to every audit engagement and the list is not necessarily complete.

(a) Characteristics of the Engagement

(i) The financial reporting framework.

(ii) Industry-specific reporting requirements such as reports mandated by industry regulators.

(iii) The expected audit coverage, including the number and locations of components to be included.

(iv) The nature of the control relationships between a parent and its components that determine how the group is to be consolidated.

(v) The extent to which components are audited by other auditors.

(vi) The entity's use of service organizations and how the auditor may obtain evidence concerning the design or operation of controls performed by them.

(vii) The expected use of audit evidence obtained in previous audits, for example, audit evidence related to risk assessment procedures and tests of controls.

(viii) The effect of information technology on the audit procedures.

(ix) The availability of client personnel and data.

(b) Reporting Objectives, Timing of the Audit, and Nature of Communications

(i) The entity's timetable for reporting.

(ii) The organization of meetings with management regarding audit work (Nature, timing and extent).

(iii) The discussion with management regarding type and timing of reports to be issued.

(iv) The discussion with management regarding communications on the status of audit work.

(v) Communication with auditors of components regarding types and timing of reports to be issued.

(vi) The nature and timing of communications among engagement team members.

(vii) Whether there are any other expected communications with third parties, including any statutory or contractual reporting responsibilities arising from the audit.

(c) Significant Factors, Preliminary Engagement Activities, and Knowledge Gained on Other Engagements

(i) The determination of materiality in accordance with SA 320.

(ii) Preliminary identification of areas where there may be a higher risk of material misstatement.

(iii) The impact of the assessed risk of material misstatement at the overall financial statement level on direction, supervision and review.

(iv) The manner in which engagement team members needs to maintain an inquisitive/ questioning mind and exercise professional skepticism and unpredictability.

(v) Results of previous audits including the identified deficiencies and action taken to address them.

(vi) The discussion of matters that may affect the audit with firm personnel responsible for performing other services to the entity.

(vii) Evidence of management's commitment to the design, implementation and maintenance of sound internal controls.

(viii) Volume of transactions which may determine reliance on internal control.

(ix) Importance attached to internal control.

(x) Significant business developments affecting the entity.

(xi) Significant industry specific developments and development in the economic environment.

(xii) Significant changes in the financial reporting framework, such as changes in accounting standards.

(xiii) Other significant relevant developments, such as changes in the legal and regulatory environment affecting the entity.

(d) Nature, Timing and Extent of Resources

(i) The selection of the engagement team and the assignment of audit work to the team members.

(ii) Engagement budgeting.

2.4 Documenting the Audit Plan

The auditor shall document-

(i) The overall audit strategy;

(ii) The audit plan; and

(iii) Any significant changes made during the audit engagement to the overall audit strategy or the audit plan, and the reasons for such changes as under-

(a) **Record of Key Decisions:** The documentation of the overall audit strategy is a record of the key decisions considered necessary to properly plan the audit and to communicate significant matters to the engagement team.

(b) **Record of Nature, Timing and Extent of Risk Assessment Procedures:** The documentation of the audit plan is a record of the planned nature, timing and extent of risk assessment procedures and additional audit procedures at the assertion level in response to the assessed risks.

(c) **Record of reasons for Change in Audit Plans:** A record of the significant changes to the overall audit strategy and the audit plan, and resulting changes to the planned nature, timing and extent of audit procedures.

2.5 Relationship between the Overall Audit Strategy and the Audit Plan

The audit strategy is prepared before the audit plan. The audit plan is more detailed than the overall audit strategy. Audit strategy and audit plan are inter-related because change in one would result into change in the other. The audit strategy provides the guidelines for developing the audit plan. It establishes the scope and conduct of the audit procedures and thereby, works as basis for developing a detailed audit plan. Detailed audit plan would include the nature, timing and extent of the audit procedures so as to obtain sufficient appropriate audit evidence.

3. AUDIT PROGRAMME

An audit programme is commonly prepared to allocate work to team members which may include the list of audit procedures and instructions to be followed by the member. It also estimates the duration for completing an audit task.

3.1 Formulating an Audit Programme

The important matters which need to be considered in this regard are:

(a) **Nature of business in which the organisation is engaged:** On his first appointment, the auditor should examine in detail the financial and accounting organisation of the business by visiting the client's office; by observing different stages through which documents pass before each transaction is authorised and recorded; the record that is kept and the type of books maintained.

The auditor, therefore, should draw up the audit programme after considering the technical, financial and accounting set-up of the company.

(b) ***Overall plan:*** *Overall plan for the audit programme should be drawn up to ensure a systematic approach to the work. If in drawing the audit programme, any divergence from the overall plan becomes necessary, first the overall plan should be modified after due consideration and thereafter, only that specific matter may be taken in the audit programme. The framework provided under the overall plan should be strictly adhered to.*

(c) ***System of internal control and accounting procedures:*** *The existence of a system of internal control ensures that both financial and statistical records are checked continuously; it also unearths errors, both of omission and of commission. The auditor, in framing his opinion on financial statements needs reasonable assurance that transactions are properly authorised and recorded in the accounting records and that transactions have not been omitted.*

(d) ***Size of the organisation and structure of its management:*** *An increase in the size of the organisation enhances the complexity of the examination of its accounting records specially when it has a number of branches, deals in several products or has a very large turnover.*

(e) ***Information as regards organisation of the business:*** *To plan audit programme, it is necessary that the auditor should obtain from his client information as regards the client's history and business, purpose and nature of engagement and time schedule for the completion of audit.*

(f) ***Accounting and management policies:*** *The auditor should review the financial statements of the past several years, audited by his predecessors specially those of the immediately preceding previous year. This would reveal to him a great deal of information regarding accounting and management policies which have been followed in the past and whether these have been employed consistently.*

3.2 Drawing up the audit programme:

The audit programme should be developed in three stages stated below:

(i) To begin with, a broad outline of the audit programme should be drawn up.

(ii) After the internal and accounting procedures have been reviewed, the details should be filled up on a consideration of the deficiencies in the system of internal control.

(iii) After the detailed checking procedure is over, the extent to which the special procedures (first time/ opening balance audit procedures) that are required to be applied should be determined. At times, special procedures may have to be applied on a consideration of the nature of business.

At each subsequent engagement, the programme should be reviewed and, if necessary, modified on account of:

(i) experience gained during the previous audits;

(ii) important changes that have taken place in the business specially in the system of internal control, accounting procedures or in the structure of management or of the scope of business; and

(iii) evaluation of internal control made for the current year.

Given below are a few circumstances where in the audit programme would have to be suitably altered:
(1) If the audit procedures were designed for a certain volume of turnover and subsequently the volume have substantially increased. Also, when there have been significant changes in the accounting organisation, procedures and personnel subsequent to the audit procedures.
(2) Where during the course of an audit, it has been discovered that internal control procedures were not as effective as assumed at the time the audit programme was framed.
(3) Where there has been an extraordinary increase in the amount of book debts or that in the value of stocks as compared to that in the previous year.
(4) When a suspicion has aroused during the course of audit or information has been received that assets of the company have been misappropriated.

4. AUDIT EXECUTION

Key phases in the audit execution stage are Execution Planning, Risk and Control Evaluation, Testing and Reporting.

4.1 Execution Planning

Prior to commencement of an audit engagement, it is important to lay down the roadmap for audit execution to ensure timely and quality audit results. The auditors need to plan their work in order to carry out the audit in an effective, efficient and timely manner.

4.2 Risk and Control Evaluation

For each segment of audit, the auditors should conduct a detailed risk and control assessment. While making Risk & Control assessment, it is necessary to bear in mind the Materiality levels as the same is linked to Audit Risks.

4.3 Testing

Once a comprehensive understanding is gained of the key risks and the controls to be evaluated in a given audit area, the auditors should test the operating effectiveness of the controls to determine whether controls are operating as designed. There are multiple test methods which can be used to arrive at the conclusions on the effectiveness of the controls.

4.4 Reporting

(Note: For details Students may refer SA 700 discussed in Chapter 6 of this study material)

4.5 Other Important Considerations

In addition to above, there are certain other consideration which auditor is required to take care while executing the audit, that are given below:

4.5.1 SA 600 - USING THE WORK OF ANOTHER AUDITOR

❖ **Principal Auditor**

- the auditor with responsibility for reporting on the financial information of an entity
- when that financial information includes the financial information of one or more components audited by another auditor.

❖ **Other Auditor**

- an auditor, other than the principal auditor,
- with responsibility for reporting on the financial information of a component which is included in the financial information audited by the principal auditor.

"Component" means a division, branch, subsidiary, joint venture, associated enterprises or other entity whose financial information is included in the financial information audited by the principal auditor.

When the principal auditor + **uses the work of another auditor** = **Principal auditor to determine how the work of the other auditor will affect the audit.**

I. ACCEPTANCE AS PRINCIPAL AUDITOR

The auditor would consider the following before accepting his work as Principal auditor:

- the materiality of the portion of the financial information which the principal auditor audits;
- the principal auditor's degree of knowledge regarding the business of the components;
- the risk of material misstatements in the financial information of the components audited by the other auditor(s); and
- the performance of additional procedures as set out in this SA regarding the components audited by other auditor(s) resulting in the principal auditor having significant participation in such audit.

II THE PRINCIPAL AUDITOR'S PROCEDURES

1. Right of Principal auditor to visit and examine books of accounts of a component
2. Principal auditor to consider the professional competence of other auditor
3. Procedures to be performed by principal auditor when using the work of other auditor

Procedures to be performed by Principal Auditor while using the work of other auditor

(a) advise the other auditor regarding use of his (other auditor) work and report and make sufficient arrangements for co-ordination at the planning stage of the audit.

(b) advise the other auditor of the significant accounting, auditing and reporting requirements and obtain representation as to compliance with them.

The principal auditor would inform the other auditor of matters such as:

- areas requiring special consideration,
- Procedures for the Identification of inter-component transactions that may require disclosure and
- the time-table for completion of audit;

4. Principal Auditor To Review - Written Summary of Other Auditor's Procedures

The principal auditor might discuss with the other auditor the audit procedures applied or review a written summary of the other auditor's procedures and findings which may be in the form of a completed questionnaire or check-list.

(i) The principal auditor may also wish to visit the other auditor.

(ii) Nature, timing and extent of procedures depend on circumstances of engagement & Materiality aspect

(iii) Nature, timing and extent of procedures depend on principal auditor's knowledge of the professional competence of the other auditor.

(iv) This knowledge may have been enhanced from the review of the previous audit work of the other auditor.

5. The principal auditor should consider the significant findings of the other auditor.

The principal auditor may consider it appropriate to discuss with the other auditor and the management of the component, the audit findings or other matters affecting the financial information of the components.

6. **When other auditor is not a professionally qualified auditor.**

In certain circumstances, the other auditor may happen to be a person other than a professionally qualified auditor.

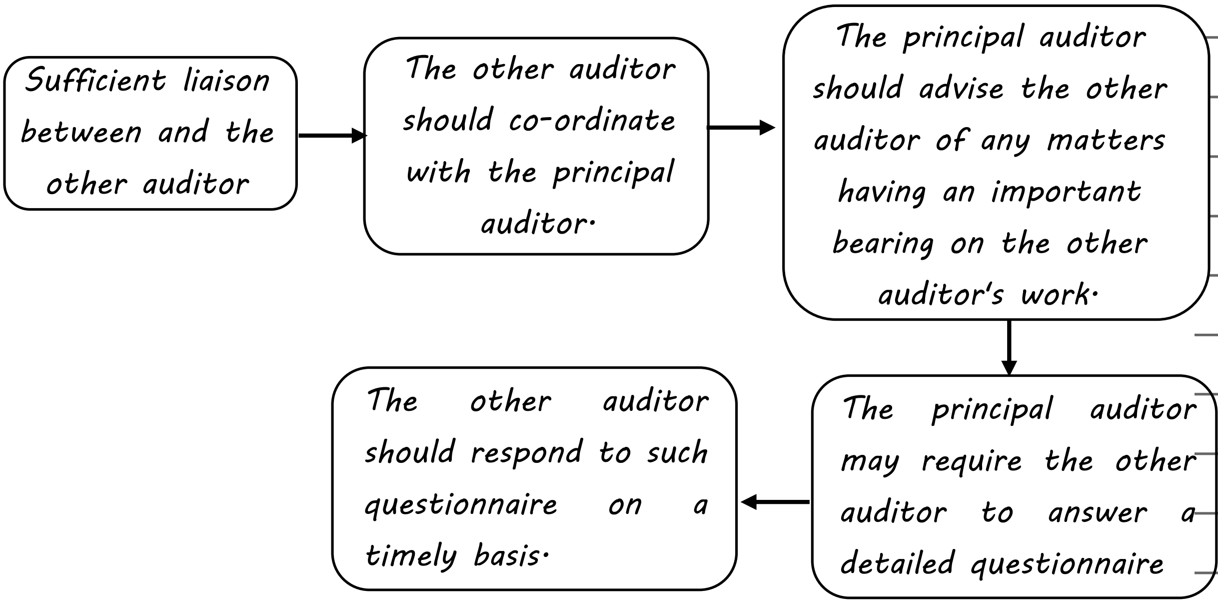
7. **Principal Auditor to document in his working papers** – the components whose financial information audited by other auditors. The principal auditor should also document the procedures performed and the conclusions reached.

III. CO-ORDINATION BETWEEN AUDITORS

There should be sufficient liaison between the principal auditor and the other auditor.

For this purpose, the principal auditor may find it necessary to issue written communication(s) to the other auditor.

Similarly, the principal auditor should advise the other auditor of any matters that come to his attention that he thinks may have an important bearing on the other auditor's work.



IV. REPORTING CONSIDERATIONS

1. Principal auditor to express a qualified opinion or disclaimer of opinion in case of a limitation on the scope of audit.
2. If the other auditor issues a Modified Report

V. DIVISION OF RESPONSIBILITY

The principal auditor would not be responsible in respect of the work entrusted to the other auditors, except in circumstances which should have aroused his suspicion about the reliability of the work performed by the other auditors.

4.5.2 SA 610- USING THE WORK OF INTERNAL AUDITORS

I. SCOPE OF THIS SA

This (SA) deals with the external auditor's responsibilities if using the work of internal auditors. This includes

(a) using the work of the internal audit function in obtaining audit evidence and

(b) using internal auditors to provide direct assistance under the direction, supervision and review of the external auditor.

This SA does not apply if the entity does not have an internal audit function.

II. THE OBJECTIVES OF THE EXTERNAL AUDITOR, WHERE THE ENTITY HAS AN INTERNAL AUDIT FUNCTION

The objectives of the external auditor, where the entity has an internal audit function		
To determine whether the work of the internal audit function or direct assistance from internal auditors can be used	If using the work of the internal audit function, to determine whether that work is adequate for purposes of the audit	If using internal auditors to provide direct assistance, to appropriately direct, supervise and review their work.

The objectives and scope of internal audit functions:

Activities Relating to Governance	Activities Relating to Risk Management	Activities Relating to Internal Control
The internal audit function may assess the governance process in its accomplishment of objectives on: • Ethics and values, performance management and accountability, • Communicating risk and control information.	• The internal audit function may assist the entity by identifying and evaluating significant exposures to risk. • The internal audit function may perform procedures to assist the entity in the detection of fraud.	• Evaluation of internal control • Examination of financial and operating information • Review of operating activities. • Review of compliance with laws and regulations.

III. EVALUATING WHETHER WORK OF THE INTERNAL AUDIT FUNCTION CAN BE USED FOR PURPOSES OF THE AUDIT

(i) The external auditor shall determine whether the work of the internal audit function can be used for purposes of the audit by evaluating the following:	**(ii) The external auditor shall not use the work of the internal audit function if the external auditor determines that:**
(a) The extent to which the internal audit function's organizational status and relevant policies and procedures support the objectivity of the internal auditors;	(a) The function's organizational status and relevant policies and procedures do not adequately support the objectivity of internal auditors;
(b) The level of competence of the internal audit function; and	(b) The function lacks sufficient competence; or
(c) Whether the internal audit function applies a systematic and disciplined approach, including quality control.	(c) The function does not apply a systematic and disciplined approach, including quality control.

IV. DETERMINING THE NATURE AND EXTENT OF WORK OF THE INTERNAL AUDIT FUNCTION THAT CAN BE USED

1. The external auditor shall consider the nature and scope of the work performed by internal audit function.

1.1 **Work of the internal audit function that can be used by the external auditor include the following:**

- Testing of the operating effectiveness of controls
- Substantive procedures involving limited judgment.
- Observations of inventory counts.
- Tracing transactions through the information system relevant to financial reporting.
- Testing of compliance with regulatory requirements.
- In some circumstances, audits or reviews of the financial information of subsidiaries that are not significant components to the group (where this does not conflict with the requirements of SA 600.

2. **The external auditor shall make all significant judgments in the audit engagement** and, to prevent undue use of the work of the internal audit function, shall plan to use less of the work of the function and perform more of the work directly:

(a)	***More judgment is involved in:***
(i)	*Planning and performing relevant audit procedures; and*
(ii)	*Evaluating the audit evidence gathered;*
(b)	*The higher the assessed risk of material misstatement at the assertion level, with special consideration given to risks identified as significant;*
(c)	*The less the internal audit function's organizational status and relevant policies and procedures adequately support the objectivity of the internal auditors; and*
(d)	*The lower the level of competence of the internal audit function.*
3.	***Extent of involvement of external auditor:*** *The external auditor shall also evaluate whether, in aggregate, using the work of the internal audit function to the extent planned would still result in the external auditor being sufficiently involved in the audit, given the external auditor's sole responsibility for the audit opinion expressed.*
4.	***Communicate how the external auditor has planned to use the work of the internal audit function:*** *The external auditor shall, in communicating with those charged with governance, share an overview of the planned scope and timing of the audit in accordance with SA 260, communicate how the external auditor has planned to use the work of the internal audit function.*

V. USING THE WORK OF THE INTERNAL AUDIT FUNCTION

1.	***Discussion and Coordination with the Internal Audit Function***
2.	*The external auditor shall* ***read the reports of the internal audit function*** *relating to the work of the function that the external auditor plans to use to obtain an understanding of the nature and extent of audit procedures it performed and the related findings.*
3.	*The external auditor* ***shall perform sufficient audit procedures to determine adequacy of internal audit function*** *for purposes of the audit, including evaluating whether:*
(a)	*The work of the function had been properly planned, performed, supervised, reviewed and documented;*
(b)	*Sufficient appropriate evidence had been obtained to enable the function to draw reasonable conclusions; and*
(c)	*Conclusions reached are appropriate in the circumstances and the reports prepared by the function are consistent with the results of the work performed.*

VI. DETERMINING WHETHER INTERNAL AUDITORS CAN BE USED TO PROVIDE DIRECT ASSISTANCE FOR PURPOSES OF THE AUDIT

(a) The external auditor prohibited from obtaining direct assistance from internal auditors.

(b) Using internal auditors to provide direct assistance is not prohibited

(i) Evaluation of the existence and significance of threats to objectivity and the level of competence of the internal auditors.

(ii) Evaluation of the existence and significance of threats shall include inquiry of the internal auditors.

In evaluating the existence and significance of threats to the objectivity of an internal auditor, the following factors may be relevant:

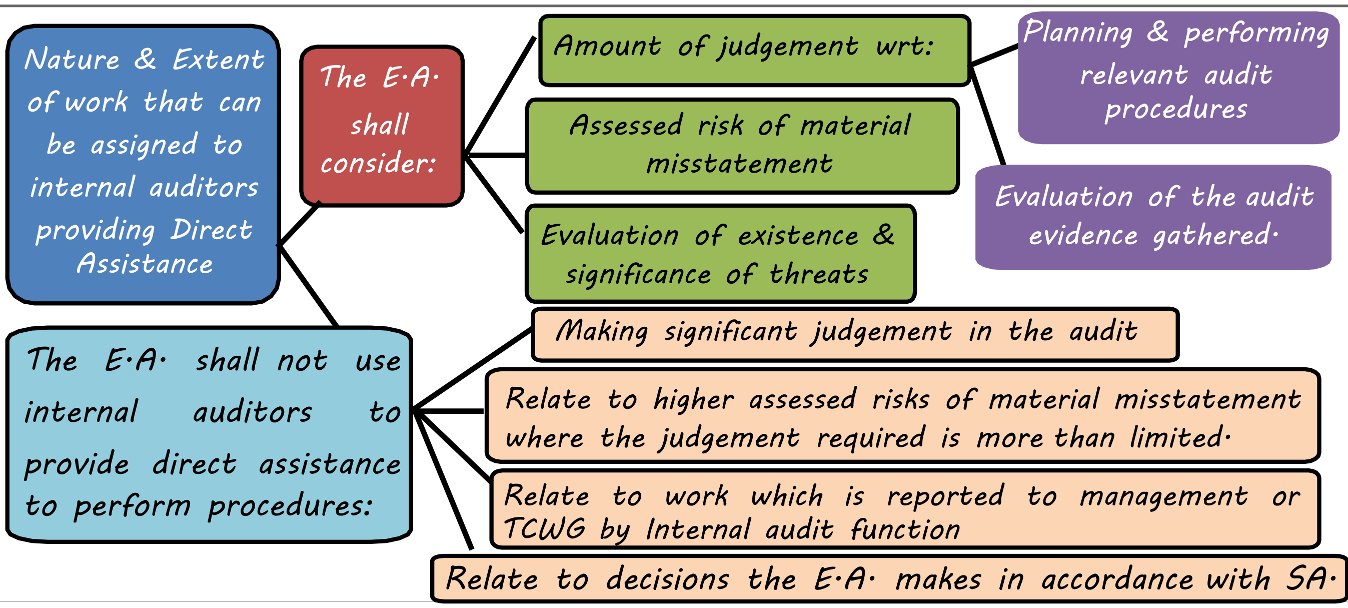
- The extent to which the internal audit function's organizational status and relevant policies and procedures support the objectivity of the internal auditors.
- Family and personal relationships with an individual working in, or responsible for, the aspect of the entity to which the work relates.
- Association with the division or department in the entity to which the work relates.
- Significant financial interests in the entity other than remuneration on terms consistent with those applicable to other employees at a similar level of seniority.

The external auditor shall not use an internal auditor to provide direct assistance if:

(a) There are significant threats to the objectivity of the internal auditor; or

(b) The internal auditor lacks sufficient competence to perform the proposed work.

Determining the Nature and Extent of Work that Can Be Assigned to Internal Auditors Providing Direct Assistance:



4.5.3 SA 620-USING THE WORK OF AN AUDITOR'S EXPERT

I. SCOPE OF SA 620

SA 620 deals with the auditor's responsibilities regarding the use of work in a field of expertise other than accounting or auditing when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence.

Auditor's Expert – An individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the auditor to assist the auditor in obtaining sufficient appropriate audit evidence. An auditor's expert may be either an auditor's internal expert (who is a partner or staff, including temporary staff, of the auditor's firm or a network firm), or an auditor's external expert.

Management's Expert – An individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements.

II THE AUDITOR'S RESPONSIBILITY FOR THE AUDIT OPINION

Expertise in a field other than accounting or auditing

- The valuation of complex financial instruments, land & buildings, plant and machinery etc.
- The actuarial calculation of liabilities
- The estimation of oil and gas reserves.
- The interpretation of contracts, laws and regulations
- The analysis of complex or unusual tax compliance issues.

III. DETERMINING THE NEED FOR AN AUDITOR'S EXPERT

An auditor's expert may be needed to assist the auditor in one or more of the following:

- Obtaining an understanding of the entity and its environment, including its internal control.
- Identifying and assessing the risks of material misstatement.
- Determining and implementing overall responses to assessed risks at the financial statement level.

- *Designing and performing further audit procedures to respond to assessed risks at the assertion level, comprising tests of controls or substantive procedures.*
- *Evaluating the sufficiency and appropriateness of audit evidence obtained in forming an opinion on the financial statements.*

IV. CONSIDERATIONS WHEN DECIDING WHETHER TO USE AN AUDITOR'S EXPERT

Considerations when deciding whether to use an auditor's expert may include:

- *Whether management has used a management's expert in preparing the financial statements.*
- *The nature and significance of the matter, including its complexity.*
- *The risks of material misstatement in the matter.*
- *The expected nature of procedures to respond to identified risks, including the auditor's knowledge of and experience with the work of experts in relation to such matters; and the availability of alternative sources of audit evidence.*

When management has used a management's expert

When management has used a management's expert in preparing the financial statements, the auditor's decision on whether to use an auditor's expert may also be influenced by such factors as:

- *The nature, scope and objectives of the management's expert's work.*
- *Whether the management's expert is employed by the entity, or is a party engaged by it to provide relevant services.*
- *The extent to which management can exercise control or influence over the work of the management's expert.*
- *The management's expert's competence and capabilities.*
- *Whether the management's expert is subject to technical performance standards or other professional or industry requirements.*
- *Any controls within the entity over the management's expert's work.*

V. NATURE, TIMING AND EXTENT OF AUDIT PROCEDURES

The nature, timing and extent of the auditor's procedures will vary depending on the circumstances. In determining the nature, timing and extent of those procedures, the auditor shall consider matters including:

(a) The nature of the matter to which that expert's work relates;

(b) The risks of material misstatement in the matter to which that expert's work relates;

(c) The significance of that expert's work in the context of the audit;

(d) The auditor's knowledge of & experience with previous work performed by that expert; and

(e) Whether that expert is subject to the auditor's firm's quality control policies and procedures.

VI THE COMPETENCE, CAPABILITIES AND OBJECTIVITY OF THE AUDITOR'S EXPERT

The auditor shall evaluate whether the auditor's expert has the necessary competence, capabilities and objectivity for the auditor's purposes. In the case of an auditor's external expert, the evaluation of objectivity shall include inquiry regarding interests and relationships that may create a threat to that expert's objectivity.

VII OTHER MATTERS THAT MAY BE RELEVANT INCLUDE

- The relevance of the auditor's expert's competence to the matter for which that expert's work will be used, including any areas of specialty within that expert's field.
- The auditor's expert's competence with respect to relevant accounting and auditing requirements
- Whether unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures indicate that it may be necessary to reconsider the initial evaluation of the competence, capabilities and objectivity of the auditor's expert as the audit progresses.

VIII EVALUATION OF THE SIGNIFICANCE OF THREATS TO OBJECTIVITY AND NEED FOR SAFEGUARDS

Evaluating the objectivity of an auditor's external expert: When evaluating the objectivity of an auditor's external expert, it may be relevant to:

(a) **Inquire of the entity** about any known interests or relationships that the entity has with the auditor's external expert that may affect that expert's objectivity.

(b) Discuss with that expert any applicable safeguards, including any professional requirements that apply to that expert; and evaluate whether the safeguards are adequate to reduce threats to an acceptable level. Interests and relationships that may be relevant to discuss with the auditor's expert include:

- Financial interests.
- Business and personal relationships.
- Provision of other services by the expert
- In some cases, it may also be appropriate for the auditor to obtain a written representation from the auditor's external expert about any interests or relationships with the entity of which that expert is aware.

IX OBTAINING AN UNDERSTANDING OF THE FIELD OF EXPERTISE OF THE AUDITOR'S EXPERT

The auditor shall obtain a sufficient understanding of the field of expertise of the auditor's expert to enable the auditor to:

(a) Determine the nature, scope and objectives of that expert's work for the auditor's purposes; and

(b) Evaluate the adequacy of that work for the auditor's purposes.

X AGREEMENT WITH THE AUDITOR'S EXPERT

The auditor shall agree, in writing when appropriate, on the following matters with the auditor's expert:

(a) The nature, scope and objectives of that expert's work;

(b) The respective roles and responsibilities of the auditor and that expert;

(c) The nature, timing and extent of communication between the auditor and that expert, including the form of any report to be provided by that expert; and

(d) The need for the auditor's expert to observe confidentiality requirements.

It is necessary for the confidentiality provisions of relevant ethical requirement that apply to the auditor also to apply to the auditor's expert. Additional requirements may be imposed by law or regulation. The entity may also have requested that specific confidentiality provisions be agreed with auditor's external experts.

XI. EVALUATING THE ADEQUACY OF THE AUDITOR'S EXPERT'S WORK

The auditor shall evaluate the adequacy of the auditor's expert's work for the auditor's purposes, including:

(a) **The relevance and reasonableness of that expert's findings or conclusions, and their consistency with other audit evidence;**

The Findings and Conclusions of the Auditor's Expert

Specific procedures to evaluate the adequacy of the auditor's expert's work for the auditor's purposes may include:

- Inquiries of the auditor's expert.
- Reviewing the auditor's expert's working papers and reports.
- Corroborative procedures, such as:
  - Observing the auditor's expert's work;
  - Examining published data, such as statistical reports from reputable, authoritative sources;
  - Confirming relevant matters with third parties;
  - Performing detailed analytical procedures to see whether Principles of materiality aspects considered; and
  - Re-performing calculations.
- Discussion with another expert with relevant expertise when, for example, the findings or conclusions of the auditor's expert are not consistent with other audit evidence.
- Discussing the auditor's expert's report with management.

(b) **If that expert's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods in the circumstances; and**

When the auditor's expert's work involves the use of significant assumptions and methods, factors relevant to the auditor's evaluation of those assumptions and methods include whether they are:

- Generally accepted within the auditor's expert's field;
- Consistent with the requirements of the applicable financial reporting framework;
- Dependent on the use of specialised models; and
- Consistent with those of management, & if not, the reason for, & effects of, the differences.

(c) **If that expert's work involves the use of source data that is significant to that expert's work, the relevance, completeness, and accuracy of that source data.**

When an auditor's expert's work involves the use of source data that is significant to that expert's work, procedures such as the following may be used to test that data:

- Verifying the origin of the data, including obtaining an understanding of, and where applicable testing, the internal controls over the data and, where relevant, its transmission to the expert.
- Reviewing the data for completeness and internal consistency

XII WHEN WORK OF THE AUDITOR'S EXPERT IS NOT ADEQUATE FOR THE AUDITOR'S PURPOSES

If the auditor determines that the work of the auditor's expert is not adequate for the auditor's purposes, the auditor shall:

(a) Agree with that expert on the nature and extent of further work to be performed by that expert; or

(b) Perform further audit procedures appropriate to the circumstances.

XIII REFERENCE TO THE AUDITOR'S EXPERT IN THE AUDITOR'S REPORT

1. The auditor shall not refer to the work of an auditor's expert in an auditor's report containing an unmodified opinion unless required by law or regulation to do so. If such reference is required by law or regulation, the auditor shall indicate in the auditor's report that the reference does not reduce the auditor's responsibility for the audit opinion.

2. If the auditor makes reference to the work of an auditor's expert in the auditor's report because such reference is relevant to an understanding of a modification to the auditor's opinion, the auditor shall indicate in the auditor's report that such reference does not reduce the auditor's responsibility for that opinion.

4.5.4. SA 540-AUDITING ACCOUNTING ESTIMATES, INCLUDING FAIR VALUE ACCOUNTING ESTIMATES & RELATED DISCLOSURES

I. SCOPE OF THIS SA

The auditor's responsibilities regarding accounting estimates, including fair value accounting estimates, + related disclosures in an audit of financial statements. = Scope of SA 540

II NATURE OF ACCOUNTING ESTIMATES

Some financial statement items cannot be measured precisely, but can only be estimated. For purposes of this SA, such financial statement items are referred to as accounting estimates.

(i) The information available to management for making of an accounting estimate varies widely,

(ii) Which affects the degree of estimation uncertainty

(iii) The degree of estimation uncertainty affects, in turn, the risks of material misstatement of accounting estimates.

(A) Some accounting estimates involve relatively low estimation uncertainty and may give rise to lower risks of material misstatements,

- Accounting estimates arising in entities that engage in business activities that are not complex.
- Accounting estimates that are frequently made and updated because they relate to routine transactions.
- Accounting estimates derived from data that is readily available.
- Fair value accounting estimates where the method of measurement prescribed by the applicable financial reporting framework is simple.
- Fair value accounting estimates where the model used to measure the accounting estimate is well-known or generally accepted.

(B) For some accounting estimates, however, there may be relatively high estimation uncertainty, particularly where they are based on significant assumptions, for example:

- Accounting estimates relating to the outcome of litigation.
- Fair value accounting estimates for derivative financial instruments not publicly traded.
- Fair value accounting estimates for which a highly specialised entity-developed model is used or for which, there are assumptions or inputs that cannot be observed in the marketplace.

III THE DEGREE OF ESTIMATION UNCERTAINTY

The degree of estimation uncertainty varies based on		
the nature of the accounting estimate,	the extent to which there is a generally accepted method used to make the accounting estimate,	the subjectivity of the assumptions used to make the accounting estimate

(A) Examples of situations where accounting estimates, other than fair value accounting estimates, may be required include:

- Allowance for doubtful accounts.
- Inventory obsolescence.
- Warranty obligations.
- Depreciation method or asset useful life.
- Provision against the carrying amount of an investment where there is uncertainty regarding its recoverability.
- Outcome of long term contracts.
- Financial Obligations / Costs arising from litigation settlements and judgments.

(B) Examples of situations where fair value accounting estimates may be required include:

- Complex financial instruments, which are not traded in an active and open market.
- Share-based payments.
- Property or equipment held for disposal.
- Certain assets or liabilities acquired in a business combination, including goodwill & intangible assets.

- Transactions involving the exchange of assets or liabilities between independent parties without monetary consideration.

IV MANAGEMENT BIAS

Financial reporting frameworks often call for neutrality, that is, freedom from bias. Accounting estimates are imprecise, however, and can be influenced by management judgment. Such judgment may involve unintentional or intentional management bias **(for example, as a result of motivation to achieve a desired result).**

The susceptibility of an accounting estimate to management bias increases with the subjectivity involved in making it.

Unintentional management bias and the potential for intentional management bias are inherent in subjective decisions that are often required in making an accounting estimate. For continuing audits, indicators of possible management bias identified during the audit of the preceding periods influence the planning and risk identification and assessment activities of the auditor in the current period.

Management bias can be difficult to detect at an account level.

- It may only be identified when considered in the aggregate of groups of accounting estimates or
- all accounting estimates, or
- when observed over a number of accounting periods.

V. THE MEASUREMENT OBJECTIVE OF ACCOUNTING ESTIMATES

The measurement objective of accounting estimates can vary depending on the applicable financial reporting framework and the financial item being reported.

VI. OBJECTIVE OF SA 540

The objective of the auditor is to obtain sufficient appropriate audit evidence whether in the context of the applicable financial reporting framework:

(a) accounting estimates, including fair value accounting estimates, in the financial statements, whether recognised or disclosed, are reasonable; and

(b) related disclosures in the financial statements are adequate.

VII. AUDITOR'S RESPONSIBILITY /AUDIT PROCEDURES

1. Risk Assessment Procedures and Related Activities for Accounting Estimates:

The auditor shall obtain an understanding of the following:

(a) The requirements of the applicable financial reporting framework relevant to accounting estimates, including related disclosures.

(b) How management identifies those transactions, events and conditions that may give rise to the need for accounting estimates to be recognised or disclosed in the financial statements. In obtaining this understanding, the auditor shall make inquiries of management about changes in circumstances that may give rise to new, or the need to revise existing, accounting estimates. As the assessment of accounting estimates affects the ultimate decision in forming an opinion, much care has to be taken in this regard. It is highly important as the Auditors conclusion is based on above basis.

2. Obtaining an Understanding of How Management Identifies the Need for Accounting Estimates:

Estimates: In preparing the financial statements, management has the responsibility to determine whether a transaction, event or condition gives rise to the need to make an accounting estimate, and that all necessary accounting estimates have been recognised, measured and disclosed in the financial statements in accordance with the applicable financial reporting framework.

Inquiries of management about changes in circumstances may include, for example, inquiries about whether:

- The entity has engaged in new types of transactions that may give rise to accounting estimates.
- Terms of transactions that gave rise to accounting estimates that have changed.
- Accounting policies relating to accounting estimates have changed, as a result of changes to the requirements of the applicable financial reporting framework or otherwise.
- Regulatory or other changes outside the control of management have occurred that may require management to revise, or make new, accounting estimates.
- New conditions or events have occurred that may give rise to the need for new or revised accounting estimates.

3. How management makes the accounting estimates: How management makes the accounting estimates, and an understanding of the data on which they are based, including:

(i) The method, including where applicable the model, used in making the accounting estimate;

(ii) Relevant controls;

(iii) Whether management has used an expert;

(iv) The assumptions underlying the accounting estimates;

(v) Whether there has been or ought to have been a change from the prior period in the methods for making the accounting estimates, and if so, why; and

(vi) Whether and, if so, how management has assessed the effect of estimation uncertainty.

The auditor shall review the outcome of accounting estimates included in the prior period financial statements, or, where applicable, their subsequent re-estimation for the purpose of the current period.

4. Estimation Uncertainty: For accounting estimates that give rise to significant risks, in addition to other substantive procedures performed to meet the requirements of SA 330, the auditor shall evaluate the following:

(a) How management has considered alternative assumptions or outcomes, and why it has rejected them

(b) Whether the significant assumptions used by management are reasonable.

(c) Where relevant to the reasonableness of the significant assumptions used by management.

(d) If, in the auditor's judgment, management has not adequately addressed the effects of estimation uncertainty on the accounting estimates that give rise to significant risks, the auditor shall, if considered necessary, develop a range with which to evaluate the reasonableness of the accounting estimate.

Recognition and Measurement Criteria: For accounting estimates that give rise to significant risks, the auditor shall obtain sufficient appropriate audit evidence whether the following are in accordance with the requirements of the applicable financial reporting framework:

(a) management's decision to recognise, or to not recognise, the accounting estimates in the financial statements; and

(b) the selected measurement basis for the accounting estimates.

I. Identifying and Assessing the Risks of Material Misstatements:

(a) In identifying and assessing the risks of material misstatement as required by SA 315, the auditor shall evaluate the degree of estimation uncertainty associated with accounting estimates.

(b) The auditor shall determine whether, in the auditor's judgment, any of those accounting estimate that have been identified as having high estimation uncertainty give rise to significant risk.

II. Responses to the Assessed Risks of Material Misstatement:

(a) Based on assessed risk of material misstatement the auditor, shall determine:

- Whether management has appropriately applied the applicable financial reporting framework relevant to the accounting estimate; and.
- Whether the methods for making the accounting estimates are appropriate and have been applied consistently

(b) In response to the assessed risk of material misstatement, the auditor shall undertake one or more of the following, taking in account the nature of the accounting estimates.

- Determine whether events occurring up to the date of the auditor's report provide sufficient audit evidence regarding the accounting estimate.
- Test checks the data used by the management for making accounting estimate.
- The auditor shall also evaluate whether the method used for measurement is appropriate in the circumstances and assumptions made by the management are reasonable in the light of the measurement objective of the applicable financial reporting. This can be achieved by

(i) Testing the extent to which data on which accounting estimate is based is accurate, complete and relevant.

(ii) Considering the source, relevance and reliability of external data.

(iii) Recalculating the accounting estimate and reviewing information.

(iv) Test checks the effectiveness of the controls

(c) While determining the matters identified or in responding to the assessed risks of material misstatement, the auditor shall consider whether specialized skills or knowledge in relation to one or more aspects of the accounting estimates are required in order to obtain sufficient appropriate audit evidence.

5. **Evaluating the Reasonableness of the Accounting Estimates, and Determining Misstatements:** The auditor shall evaluate, based on the audit evidence, whether the accounting estimates in the financial statements are either reasonable in the context of the applicable financial reporting framework, or are misstated.

VIII. AUDIT REPORTING & DISCLOSURE:

Disclosures Related to Accounting Estimates

(a) The presentation of financial statement in accordance with the applicable financial reporting framework includes adequate disclosure of material matters. These disclosures may include, • The assumptions used. • The method of estimation used, including any applicable model. • The basis for the selection of the estimation. • Any changes in the method of estimation from prior period and its subsequent effect. • The sources and implication of estimation uncertainty.	**(b)** In relation to accounting estimate having significant risk, even where the disclosures are in accordance with the applicable financial reporting framework, the auditor may conclude that the disclosure of estimation uncertainty is inadequate in light of the circumstances and facts involved.

Written Representations: The auditor shall obtain written representations from management and, where appropriate, those charged with governance whether they believe significant assumptions used in making accounting estimates are reasonable.

4.5.5 ANALYTICAL PROCEDURES PRIOR TO AUDIT AS WELL AS TOWARDS FINALIZATION

1. WHEN DESIGNING AND PERFORMING SUBSTANTIVE ANALYTICAL PROCEDURES

As per SA 520, "Analytical Procedures" the auditor shall:

(a) Determine the suitability of particular substantive analytical procedures for given assertions, taking account of the assessed risks of material misstatement and tests of details, if any, for these assertions;

(b) Evaluate the reliability of data from which the auditor's expectation of recorded amounts or ratios is developed, taking account of source, comparability, and nature and relevance of information available, and controls over preparation;

(c) Develop an expectation of recorded amounts or ratios and evaluate whether the expectation is sufficiently precise to identify a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated; and

(d) Determine the amount of any difference of recorded amounts from expected values that is acceptable without further investigation as required.

II. ANALYTICAL PROCEDURES THAT ASSIST WHEN FORMING AN OVER ALL CONCLUSION

(a) The auditor shall design and perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion as to whether the financial statements are consistent with the auditor's understanding of the entity.

(b) The conclusions drawn from the results of analytical procedures designed and performed in accordance with above are intended to verify conclusions formed during the audit of individual components or elements of the financial statements. This assists the auditor to draw reasonable conclusions on which to base the auditor's opinion.

(c) The results of such analytical procedures may identify a previously unrecognised risk of material misstatement. In such circumstances, SA 315 requires the auditor to revise the auditor's assessment of the risks of material misstatement and modify the further planned audit procedures accordingly.

(d) The analytical procedures performed in accordance with above may be similar to those that would be used as risk assessment procedures.

III. INVESTIGATING RESULTS OF ANALYTICAL PROCEDURES

If analytical procedures performed in accordance with this SA 520 identify fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount, the auditor shall investigate such differences by:

(a) Inquiring of management and obtaining appropriate audit evidence relevant to management's responses; and

(b) Performing other audit procedures as necessary in the circumstances: The need to perform other audit procedures may arise when, for example, management is unable to provide an explanation, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate.

4. MATERIALITY, RISK ASSESSMENT AND INTERNAL CONTROL

1. MATERIALITY & RISK ASSESSMENT

As per SA 320, the concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report. Materiality and audit risk are considered throughout the audit, in particular, when identifying and assessing the risks of material misstatement, determining the nature, timing and extent of further audit procedures; and evaluating the effect of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report.

1.1 Identification of Risks

Audit risk is the risk of expressing an inappropriate audit opinion on financial statements that are materially misstated.

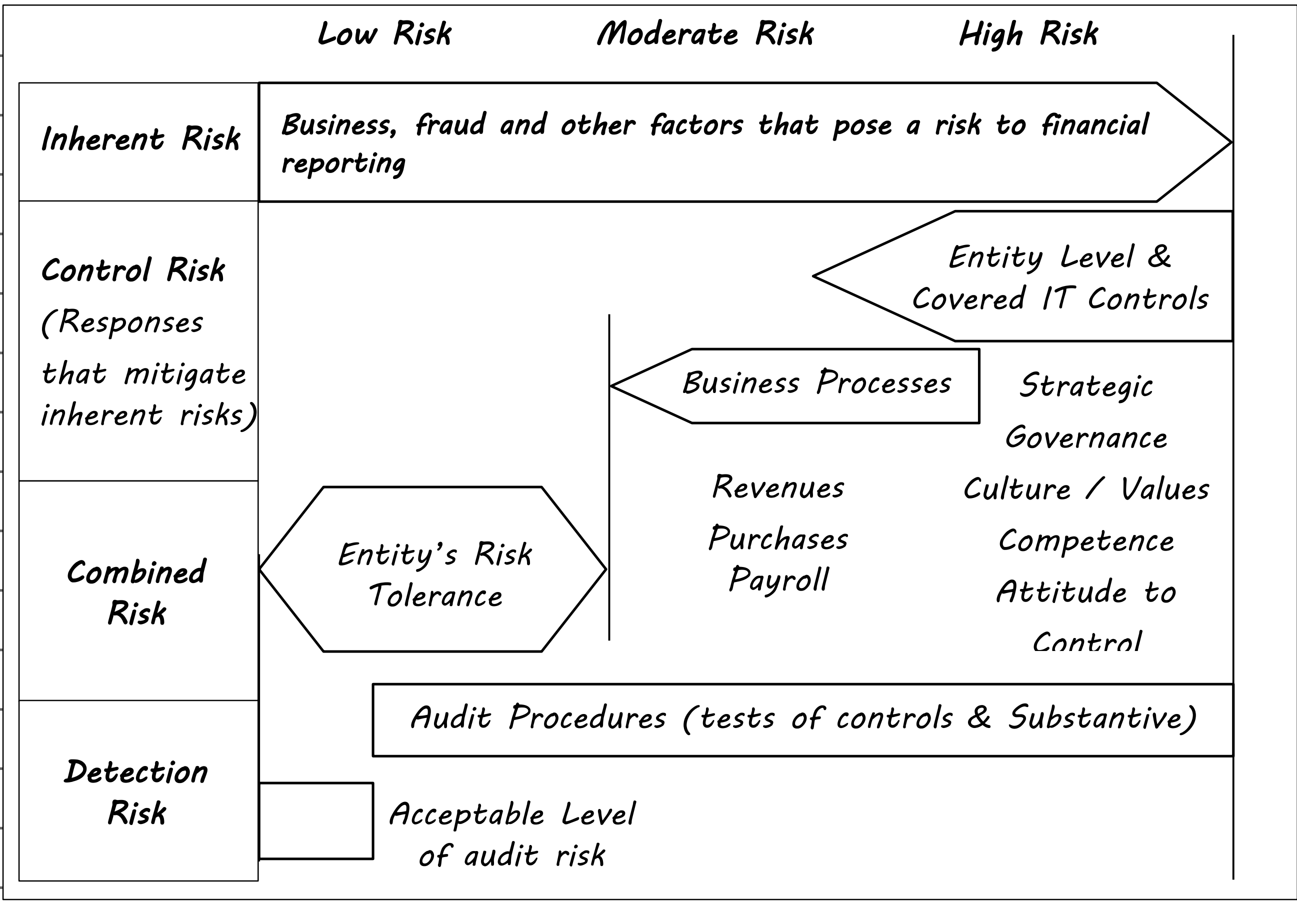
1.2 Audit Risk Components

The major components of audit risk are described in the Table below

Nature	Description
Inherent Risk	Susceptibility of an assertion to a misstatement that could be material, individually or when aggregated with other misstatements, assuming that there are no related controls. Inherent risk is addressed at both the financial statement level and at the assertion level. For example, technological developments might make a particular product obsolete, thereby causing inventory to be more susceptible to overstatement.

Control Risk (Do internal controls in place mitigate the inherent risks?)	*Risk that the entity's internal control system will not prevent, or detect and correct on a timely basis, a misstatement that could be material, individually or when aggregated with other misstatements.*
Detection Risk	*This is the risk that the auditor will not detect a misstatement that exists in an assertion that could be material, either individually or when aggregated with other misstatements. The acceptable level of detection risk for a given level of audit risk bears an inverse relationship to the risks of material misstatement at the assertion level*

Interrelationship of Audit Risk Components



Risks of Material Misstatement

Mathematically Audit Risk (AR) can be expressed as a product of Inherent Risk (IR), Control Risk (CR) and Detection Risk (DR), i.e. AR = IR x CR x DR

Audit Risk has two components: *Risk of material misstatement (the risk that the financial statements contain a material misstatement) and detection risk (the risk that the auditor will not be able to detect such misstatement).*

The relationship can be defined as follows.

Audit Risk = Risk of Material Misstatement X Detection Risk
Risk of material Misstatement: - Risk of material misstatement is anticipated risk that a material misstatement may exist in financial statement before start of the audit. It has two components inherent risk and control risk. The relationship can be defined as Risk of material Misstatement = Inherent risk X Control risk
Detection risk: It is a risk that a material Misstatement remained undetected even if all Audit procedures applied.
It should be noted that the combined level of Inherent Risk and Control Risk is inversely related with Detection Risk, and Audit Materiality is also inversely related with audit risk.

SA 315, "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment" categorises the types of assertions used by the auditor to consider the different types of potential misstatements that may occur, as follows:

Assertions about classes of transactions and events for the period under audit:	*(i) Occurrence -*	*transactions and events that have been recorded have occurred and pertain to the entity.*
	(ii) Completeness	*all transactions and events that should have been recorded*
	(iii) Accuracy—	*amounts and other data relating to recorded transactions and events have been recorded appropriately.*
	(iv) Cut-off—	*transactions and events have been recorded in the correct accounting period.*
	(v) Classification-	*transactions and events have been recorded in the proper accounts.*
Assertions about account balances at the period end:	*(i) Existence—*	*assets, liabilities, and equity interests exist.*

	(ii) Rights and obligations—	the entity holds or controls the rights to assets, and liabilities are the obligations of the entity.
	(iii) Completeness—	all assets, liabilities and equity interests that should have been.
	(iv) Valuation and allocation—	assets, liabilities, and equity interests are included in the FS at appropriate amounts and any resulting valuation or allocation adjustments are appropriately recorded.
Assertions about presentation and disclosure:	(i) Occurrence and rights and obligations —	disclosed events, transactions, and other matters have occurred and pertain to the entity.
	(ii) Completeness—	all disclosures that should have been included in the financial statements have been included.
	(iii) Classification and understandability—	financial information is appropriately presented and described, and disclosures are clearly expressed.
	(iv) Accuracy and valuation—	financial and other information are disclosed fairly and at appropriate amounts."

Auditors are required to assess the risks of material misstatement at two levels. The first is at the overall financial statement level, which refers to risks of material misstatement that relate pervasively to the financial statements as a whole and potentially affect many assertions.

1.3 Steps for Risk Identification

- Assess the significance of the assessed risk, impact of its occurrence and also revise the materiality accordingly for the specific account balance.

- Determine the likelihood for assessed risk to occur and its impact on our auditing procedures.
- Document the assertions that are effected.
- Consider the impact of the risk on each of the assertions
- (completeness, existence, accuracy, validity, valuation and presentation) relevant to the account balance, class of transactions, or disclosure.
- Identify the degree of significant risks that would require separate attention and response by the auditor. Planned audit procedures should directly address these risks.
- Enquire and document the management's response.
- Consider the nature of the internal control system in place and its possible effectiveness in mitigating the risks involved. Ensure the controls:
  - Routine in nature (occur daily) or periodic such as monthly.
  - Designed to prevent or detect and correct errors.
  - Manual or automated.
- Consider any unique characteristics of the risk.
- Consider the existence of any particular characteristics (inherent risks) in the class of transactions, account balance or disclosure that need to be addressed in designing further audit procedures.

Possible potential misstatements – Indicators

Completeness	Existence	Recording	Cut-Off Procedure
• Transactions not identified. • Source documents not prepared. • Source documents not captured. • Rejected source documents not represented	• Fictitious or unauthorised transactions entered on source documents. • Source documents overstated. • Transactions duplicated on source documents. • Capture of source documents duplicated. • Invalid source documents captured on subsidiary ledgers.	• Source documents captured inaccurately. • Processing of transactions is inaccurate. • Inaccurate adjustments made in subsidiary ledgers.	• Transactions that occur in one period are recorded in another period.

2. RISK-BASED AUDIT APPROACH

Audit should be risk-based or focused on areas of greatest risk to the achievement of the audited entity's objectives. Risk-based audit (RBA) is an approach to audit that analyzes audit risks, sets materiality thresholds based on audit risk analysis and develops audit programmes that allocate a larger portion of audit resources to high-risk areas.

2.1 Audit Risk Analysis

The auditor should perform an analysis of the audit risks that impact on the auditee before undertaking specific audit procedures. Risk assessment is a subjective process. It is part of the professional judgment of the auditor and of the particular circumstances. It is the risk that the auditor may unknowingly fail to appropriately modify his opinion on financial statements that are materially misstated.

Audit risks are brought about by error and fraud:
♦ Error is an unintentional mistake resulting from omission, as when legitimate transactions and/or balances are excluded from the financial statements; or by commission, as when erroneous transactions and/or balances are included in the financial statements.
♦ Fraud is an intentional misstatement in the accounting records or supporting documents from which the financial statements are prepared. It is intended to deceive financial statement users or to conceal misappropriations.

2.2 General Steps in the Conduct of Risk Based Audit

This involves the following three key steps:

- Assessing the risks of material misstatement in the financial statements
- Designing and performing further audit procedures that respond to assessed risks and reduce the risks of material misstatements in the financial statements to an acceptably low level; and
- Issuing an appropriate audit report based on the audit findings.

The risk-based audit process is presented in three distinct phases:

- Risk assessment.
- Risk response; and
- Reporting

2.2.1 Risk Assessment

The risk assessment phase of the audit involves the following steps:

- Performing client acceptance or continuance procedures;
- Planning the overall engagement;
- Performing risk assessment procedures to understand the business and identify inherent and control risks;
- Identifying relevant internal control procedures and assessing their design and implementation.
- Assessing the risks of material misstatement in the financial statements;
- Identifying the significant risks that require special audit consideration.
- Communicating any material weaknesses in the design and implementation.
- Making an informed assessment of the risks of material misstatement at the financial statement level and at the assertion level.

2.2.2 Risk response

Some of the matters the auditor should consider when planning the audit procedures include:

- ♦ Assertions that cannot be addressed by substantive procedures alone. This can occur where there is highly automated processing of transactions with little or no manual intervention.
- ♦ Existence of internal control that, if tested, could reduce the need/scope for other substantive procedures.
- ♦ The potential for substantive analytical procedures that would reduce the need/scope for other types of procedures.
- ♦ The need to incorporate an element of unpredictability in procedures performed.
- ♦ The need to perform further audit procedures to address the potential for management override of controls or other fraud scenarios.
- ♦ The need to perform specific procedures to address "significant risks" that have been identified.

Audit procedures designed to address the assessed risks could include a mixture of:

- ♦ Tests of the operational effectiveness of internal control; and

- Substantive procedures such as tests of details and analytical procedures.

2.2.3 Reporting

It is important at this stage to determine:

- If there had been a change in the assessed level of risk;
- Whether conclusions drawn from work performed are appropriate; and
- If any suspicious circumstances have been encountered.

Any additional risks should be appropriately assessed, and further audit procedures performed as required.

When all procedures have been performed and conclusions reached:

- Audit findings should be reported to management and those charged with governance; and
- An audit opinion should be formed, and a decision made on the appropriate wording for the auditor's report.

3. INTERNAL CONTROL SYSTEM - NATURE, SCOPE, OBJECTIVES AND STRUCTURE

"Internal Control System" means all the policies and procedures (internal controls) adopted by the management of an entity to assist in achieving management's objective of ensuring, as far as practicable, the orderly and efficient conduct of its business, including adherence to management policies, the safeguarding of assets, the prevention and detection of fraud and error, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information.

The following are the Nature, Scope, Objectives and Structure of an Internal Control System:

3.1 Nature of Internal Control

Internal control is a process/set of processes designed to facilitate and support the achievement of business objectives.

3.2 Scope of Internal Controls

The scope of internal controls extends beyond mere accounting controls and includes all administrative controls concerned with the decision - making process leading to managements authorization of transaction, such controls include, production method, time and motion study, pricing policies, quality control, work standard, budgetary control, policy appraisal, quantitative controls etc.

INTERNAL CONTROL SYSTEM

- Facilitates the effectiveness and efficiency of operations.
- Helps ensure the reliability of internal and external financial reporting.
- Assists compliance with laws and regulations.
- Helps safeguarding the assets of the entity.

3.3 Objectives of Internal Control System

The objectives of internal controls relating to the accounting systems are:	
(i)	Transactions are executed through general or specific management **authorization**.
(ii)	All transactions are **promptly recorded** in an appropriate manner to permit the preparation of financial information and to maintain accountability of assets.
(iii)	Assets and records are **safeguarded from unauthorized access, use or disposition**
(iv)	Assets are **verified at reasonable intervals and appropriate action** is taken with regard to the **discrepancies**.

Precisely, the control objectives ensure that the transactions processed are complete, valid and accurate. The basic accounting control objectives which are sought to be achieved by any accounting control system are:

Ensure all transactions are

- Recorded
- Real
- Properly Valued
- Recorded Timely
- Properly Posted
- Properly Classified and Disclosed
- Properly Summarized

If the response to all the above answer is positive, the auditor would be justified in limiting his account balance tests considerably.

In the case of excellent companies, where in a system a particular control is found to be deficient, audit attention can be focused on the areas where basic accounting control objectives are not being adhered to

3.3.1 **Limitations of Internal Control -** Internal control, no matter how effective, can provide an entity with only reasonable assurance and not absolute assurance about achieving the entity's operational, financial reporting and compliance objectives.

Internal control systems are subject to certain inherent limitations, such as:

- Management's consideration that the cost of an internal control does not exceed the expected benefits to be derived.
- The fact that most internal controls do not tend to be directed at transactions of unusual nature. The potential for human error, such as, due to carelessness, distraction, mistakes of judgement and misunderstanding of instructions.
- The possibility of circumvention of internal controls through collusion with employees or with parties outside the entity.
- The possibility that a person responsible for exercising an internal control could abuse that responsibility.
- Manipulations by management with respect to transactions or estimates.

3.4 Structure of Internal Control

In order to achieve the objectives of internal controls, it is necessary to establish adequate control policies and procedures. Most of these policies and procedures cover:

3.4.1 **Segregation of duties-** Transaction processing are allocated to different persons in such a manner that no one person can carry through the completion of a transaction from start to finish or the work of one person is made complimentary to the work of another person. The purpose is to minimize the occurrence of fraud and errors and to detect them on a timely basis, when they take place. The following functions are segregated-

(a) authorization of transactions;

(b) execution of transactions;

(c) physical custody of related assets; and

(d) maintenance of records and documents

3.4.2 ***Authorization of Transaction-*** *Delegation of authority to different levels and to particular persons are required to establish by the management for controlling the execution of transaction in accordance with prescribed conditions. Authorization may be general or it may be specific with reference to a single transaction.*

3.4.3 ***Adequacy of Records and Documents -*** *Accounting controls should ensure that -*

(i)	*Transactions are executed in accordance with management's general or specific authorization.*
(ii)	*Transactions and other events are promptly recorded at correct amounts.*
(iii)	*Transactions should be classified in appropriate accounts and in the appropriate period to which it relates.*
(iv)	*Transaction should be recorded in a manner so as to facilitate preparation of financial statements in accordance with applicable accounting standards, other accounting policies and practices and relevant statutory requirements.*
(v)	*Recording of transaction should facilitate maintaining accountability for assets.*
(vi)	*Assets and records are required to be protected from unauthorized access, use or disposition.*
(vii)	*Records of assets such as sufficient description of the assets (to facilitate identification) its location should also be maintained so that the assets could be physically verified periodically.*

3.4.4 ***Accountability and Safeguarding of Assets -*** *The process of accountability of assets commences from acquisitions of assets its use and final disposal. Safeguarding of assets requires appropriate maintenance of records, their periodic reconciliation with the related assets.*

3.4.5 ***Independent Checks -****Independent verification of the control systems, designed and implemented by the management, involves periodic or regular review by independent persons to ascertain whether the control procedures are operating effectively or not. Such process may be carried out by specially assigned staff under the banner of external audit.*

4. COMPONENTS OF INTERNAL CONTROLS

Components of Internal Control

- Control environment
- Entity's risk assessment process
- Control activities
- Information system and communication
- Monitoring of controls

4.1 Control Environment

The control environment encompasses the following elements:

(a) **Communication and enforcement of integrity and ethical values:** The effectiveness of controls cannot rise above the integrity and ethical values of the people who create, administer, and monitor them. Integrity and ethical behavior are the product of the entity's ethical and behavioral standards, how they are communicated, and how they are reinforced in practice.

(b) **Commitment to competence:** Competence is the knowledge and skills necessary to accomplish tasks that define the individual's job.

(c) **Participation by those charged with governance:** An entity's control consciousness is influenced significantly by those charged with governance. The importance of the responsibilities of those charged with governance is recognised in codes of practice and other laws and regulations or guidance produced for the benefit of those charged with governance.

(d) **Management's philosophy and operating style:** Management's philosophy and operating style encompass a broad range of characteristics.

(e) **Organisational structure:** Establishing a relevant organizational structure includes considering key areas of authority and responsibility and appropriate lines of reporting.

(f) **Assignment of authority and responsibility:** The assignment of authority and responsibility may include policies relating to appropriate business practices, knowledge and experience of key personnel, and resources provided for carrying out duties.

(g) **Human resource policies and practices:** Human resource policies and practices often demonstrate important matters in relation to the control consciousness of an entity.

4.2 **Entity's Risk Assessment Process**

For financial reporting purposes, the entity's risk assessment process includes how management identifies business risks relevant to the preparation of financial statements in accordance with the entity's applicable financial reporting framework, estimates their significance, assesses the likelihood of their occurrence, and decides upon actions to respond to and manage them and the results thereof.

Risks can arise or change due to circumstances such as the following:
(a) Changes in operating environment. Changes in the regulatory or operating environment can result in changes in competitive pressures and significantly different risks.
(b) New personnel. New personnel may have a different focus on or understanding of internal control.
(c) New or revamped information systems. Significant and rapid changes in information systems can change the risk relating to internal control.
(d) Rapid growth. Significant and rapid expansion of operations can strain controls and increase the risk of a breakdown in controls.
(e) New technology. Incorporating new technologies into production processes or information systems may change the risk associated with internal control.
(f) New business models, products, or activities. Entering into business areas or transactions with which an entity has little experience may introduce new risks associated with internal control.
(g) Corporate restructurings. Restructurings may be accompanied by staff reductions and changes in supervision and segregation of duties that may change the risk associated with internal control.
(h) Expanded foreign operations. The expansion or acquisition of foreign operations carries new and often unique risks that may affect internal control, for example, additional or changed risks from foreign currency transactions.
(i) New accounting pronouncements. Adoption of new accounting principles or changing accounting principles may affect risks in preparing financial statements.

4.3 **Control Activities**

Generally, control activities that may be relevant to an audit may be categorised as policies and procedures that pertain to the following:

(a) **Performance reviews:** These control activities include reviews and analyses of actual performance versus budgets, forecasts, and prior period performance; relating different sets of data - operating or financial - to one another, together with analyses of the relationships and investigative and corrective actions; comparing internal data with external sources of information; and review of functional or activity performance.

(b) Information processing: The two broad groupings of information systems control activities are application controls, which apply to the processing of individual applications, and general IT-controls, which are policies and procedures that relate to many applications and support the effective functioning of application controls by helping to ensure the continued proper operation of information systems.

(c) Physical controls: Controls that encompass:

- The physical security of assets, including adequate safeguards such as secured facilities over access to assets and records.
- The authorisation for access to computer programs and data files.
- The periodic counting and comparison with amounts shown on control records

(d) Segregation of duties: Assigning different people the responsibilities of authorising transactions, recording transactions, and maintaining custody of assets.

4.4 Information System, Including the Related Business Processes, Relevant to Financial Reporting, and Communication

An information system consists of infrastructure (physical and hardware components), software, people, procedures, and data. Many information systems make extensive use of information technology (IT).

The information system relevant to financial reporting objectives, which includes the financial reporting system, encompasses methods and records that:

(a) Identify and record all valid transactions.

(b) Describe on a timely basis the transactions in sufficient detail to permit proper classification of transactions for financial reporting.

(c) Measure the value of transactions in a manner that permits recording their proper monetary value in the financial statements.

(d) Determine the time period in which transactions occurred to permit recording of transactions in the proper accounting period.

(e) Present properly the transactions & related disclosures in the financial statements.

Communication, which involves providing an understanding of individual roles and responsibilities pertaining to internal control over financial reporting, may take such forms as policy manuals, accounting and financial reporting manuals, and memoranda. Communication also can be made electronically, orally, and through the actions of management.

4.5 Monitoring of Controls

An important management responsibility is to establish and maintain internal control on an ongoing basis. Management's monitoring of controls includes considering whether they are operating as intended and that they are modified as appropriate for changes in conditions. Monitoring of controls may include activities such as, management's review of whether bank reconciliations are being prepared on a timely basis, internal auditors' evaluation of sales personnel's compliance with the entity's policies on terms of sales contracts, and a legal department's oversight of compliance with the entity's ethical or business practice policies. Monitoring is done also to ensure that controls continue to operate effectively over time. For example, if the timeliness and accuracy of bank reconciliations are not monitored, personnel are likely to stop preparing them.

The overall systems of internal control comprises of Administrative Control and Accounting Controls, Internal Checks and Internal Audit are important constituents of Accounting Controls.

1. **Internal Check System -** Internal check system implies organization of the overall system of book-keeping and arrangement of Staff duties in such a way that no one person can carry through a transaction and record every aspect thereof. It is a part of overall control system and operates basically as a built-in-device as far as organization and job-allocation aspects of the controls are concerned.

The following are the objectives of the internal check system:

(i) To detect error and frauds with ease.

(ii) To avoid & minimize the possibility of commission of errors & fraud by any staff.

(iii) To increase the efficiency of the staff working within the organization.

(iv) To locate the responsibility area or the stages where actual fraud and error occurs.

(v) To protect the integrity of the business by ensuring that accounts are always subject to proper scrutiny and check.

(vi) To prevent and avoid the misappropriation or embezzlement of cash and falsification of accounts.

The effectiveness of an efficient system of internal check depends on the following considerations-

(i) **Clarity of Responsibility** - The responsibility of different persons engaged in various operations of business transactions should be properly identified.

(ii) **Division of Work** - The segregation of work should be made in such a manner that the free flow of work is not interrupted and also helps to determine that the work of one person is complementary to the other.

(iii) **Standardization** - The entire process of accounting should be standardized by creating suitable policies commensurate with the nature of the business, so as to strengthen the system of internal check.

(iv) **Appraisal** - Periodic review should be made of the chain of operations and work flow. Such process may be carried out by preparing an audit flow chart.

The general condition pertaining to the internal check system may be summarized as under:

(i) no single person should have complete control over any important aspect of the business operation. Every employee's action should come under the review of another person.

(ii) Staff duties should be rotated from time to time so that members do not perform the same function for a considerable length of time.

(iii) Every member of the staff should be encouraged to go on leave at least once a year.

(iv) Persons having physical custody of assets must not be permitted to have access to the books of accounts.

(v) There should exist an accounting control in respect of each class of assets, in addition, there should be periodical inspection so as to establish their physical condition.

(vi) Mechanical devices should be used, where ever practicable to prevent loss or misappropriation of cash.

(vii)	Budgetary control should be exercised and wide deviations observed should be reconciled.
(viii)	For inventory taking, at the close of the year, trading activities should, if possible be suspended, and it should be done by staff belonging to several sections of the organization.
(ix)	The financial and administrative powers should be distributed very judiciously among different officers and the manner in which those are actually exercised should be reviewed periodically.
(x)	Procedures should be laid down for periodical verification and testing of different sections of accounting records to ensure that they are accurate.

The scope of statutory audit is limited by both time and cost. Therefore, it is increasingly being recognized that for an audit to be effective especially in case of large organization, the existence of a system of internal check is essential.

2. **Internal Audit -** Internal audit may be defined as, an independent appraisal function established within an organization to examine and evaluate its activities as a service to the organization. The scope of the internal audit is determined by the management.

5. REVIEW OF THE SYSTEM OF INTERNAL CONTROLS

Manual elements in internal control may be more suitable where judgment and discretion are required such as for the following circumstances:

- Large, unusual or non-recurring transactions.
- Circumstances where errors are difficult to define, anticipate or predict.
- In changing circumstances that require a control response outside the scope of an existing automated control.
- In monitoring the effectiveness of automated controls.

The extent & nature of the risks to internal control vary depending on the nature & characteristics of the entity's information system. The entity responds to the risks arising from the use of IT or from use of manual elements in internal control by establishing effective controls in light of the characteristics of the entity's information system.

The review of the internal control system enables the auditor -

(i) to formulate his opinion as to the reliance he may place on the system itself

(ii) to locate the areas of weakness in the system so that the audit programme and the nature, timing and extent of substantive and compliance audit procedures can be adjusted to meet the situation.

Deciding the point of time appropriate for undertaking the review of the internal controls is a matter for individual judgement of the auditor. This decision can be taken on a consideration of the size and complexity of the client's operations. If the auditor, because of his continuing relationship with his client, is already aware of the features and efficacy of internal controls, he may just review the changes that have taken place in the intervening period because of changes in the operations of the client. However, a comprehensive review in such cases must be made at an interval of, say, 3 years.

When the auditor finds inadequacies or weaknesses in the internal control system, he should advise his client about such inadequacies and weaknesses and the consequences that may follow. It should be the duty of the auditor to see, in the course of his audit, how far the inadequacies and weaknesses have been removed. He will take this into account in preparing his audit report. It is a useful practice to note the following after each function, set out in the audit programme –

(a) Any change in the system of internal control from that record in the appropriate section of the internal control questionnaire

(b) Any further weakness noted in the internal control.

(c) Any instance where the prescribed system or procedure has not been followed.

These should be considered in deciding whether any further modification in the audit programme is called for. Also, these should be communicated to the client and confirmation should be sought as regards changes in the system.

6. INTERNAL CONTROL ASSESSMENT & EVALUATION

The quality & effectiveness of internal controls is directly dependent on the organisational environment. The tone at the top (the Board & Executive Management) & the credibility of the message on internal controls from top plays an important role in establishing strong control environment. Following are some of the key components to assess & evaluate the controls environment:

Standard Operating Procedures (SOPs): A well defined set of SOPs helps define role, responsibilities, process & controls & thus helps clearly communicate the operating controls to all touch points of a process. The controls are likely to be clearly understood & consistently applied even during employee turnover.

1. **Enterprise Risk Management:** An organization which has robust process to identify & mitigate risks across the enterprise & its periodical review will assist in early identification of gaps & taking effective control measures. In such organizations, surprises of failures in controls is likely to be few.
2. **Segregation of Job Responsibilities:** A key element of control is that multiple activities in a transaction/decision should not be concentrated with one individual. Segregation of duties is an important element of control such that no two commercial activities should be conducted by the same person.
3. **Job Rotation in Sensitive Areas:** Any job carried out by the same person over a long period of time is likely to lead to complacency & possible misuse in sensitive areas. It is therefore important that in key commercial functions, the job rotation is regularly followed to avoid degeneration of controls.
4. **Delegation of Financial Powers Document:** As the organization grows, it needs to delegate the financial & other powers to their employees. A clearly defined document on delegation of powers allows controls to be clearly operated without being dependent on individuals.
5. **Information Technology based Controls:** With the advent of computers & enterprise resource planning (ERP) systems, it is much easier to embed controls through the system instead of being human dependent. The failure rate for IT embedded controls is likely to be low, is likely to have better audit trail & is thus easier to monitor.

6.1 Techniques of evaluation of Internal control

The following are the techniques of evaluation of internal control:

6.1.1 Questionnaire

Most of the auditing firms have developed their own standardised internal control questionnaire on a generally applicable basis. A questionnaire is a set of questions framed in an organised manner, about each functional area, which has as purpose the evaluation of the effectiveness of control and detection of its weakness if any. A questionnaire usually consists of several separate sections devoted to areas such as purchases, sales, trade receivables, trade payables, wages, etc. The questionnaire is intended to be filled by the company executives who are in charge of the various areas. However, this poses some practical difficulties. The questionnaire is to travel from executives and, therefore, it may take a pretty long time to be filled; also the questions may not be readily intelligible to busy executives and there is a possibility of the questionnaire being misplaced while travelling from one table to another. Having regard to these difficulties, it is now almost an accepted practice that the auditor (or his representative) arranges meetings with the executives concerned and gets the answers filled by each executive. Sometimes, the auditor himself may be required to fill the answers. In such a case, he should ensure that the concerned executive has initiated the answers as a token of his agreement therewith.

Questions are so framed as generally to dispense with the requirement of a detailed answer to each question. For this purpose, often one general question is broken down into a number of questions and sub-questions to enable the executive to provide a just 'Yes', 'No' or 'Not applicable' form of reply. Questions are also framed in such a manner that generally a "No" answer will reflect weakness in the control system. This requires giving a positive power to the question, keeping in view what the proper control should be.

In the use of standardized internal control questionnaire, certain basic assumptions about elements of good control are taken into account. These are -
(i) Certain procedures in general used by most business concerns are essential in achieving reliable internal control. This is a time-tested assumption.

(ii)	Organisations are such that permit an extensive division of duties and responsibilities. The larger the organisation, the greater is the scope of such division.
(iii)	Employees concerned with accounting function are not assigned any custodial function.
(iv)	No single person is thrust with the responsibility of completing a transaction all by himself.
(v)	There should always be evidence to identify the person who has done the work whether involving authorisation, implementation or checking.
(vi)	The work performed by each one is expected to come under review of another in the usual course of routine.
(vii)	There is proper documentation and recording of the transactions.

For the first year of engagements, issue of questionnaire is necessary.

For subsequent years, the auditor, instead of issuing a questionnaire again, may request the client to confirm whether any change in the nature and scope of business has taken place that necessitated a corresponding change in the control system, or whether, even without a change in the nature and scope of business, the control system has undergone a change.

If there has been a change, the auditor should take note of its and enter appropriate comments on the relevant part of the questionnaire. However, it would be a good practice in the case of continuing engagements to issue a questionnaire irrespective of any change, say, every third year. This will obviate unnecessary trouble of filling the answers every time and to that extent the client's and the auditor's own time will be saved.

6.1.2 Check List

It is a series of instructions or questions on internal control which the auditor must follow or answer. When a particular instruction is carried out, the auditor initials the space opposite the instruction. If it is in the form of a question, the answer generally 'Yes', 'No' or 'Not Applicable' is entered opposite the question. A check list is more in the nature of a reminder to the auditor about the matters to be checked for testing the internal control system. The question form of check list may even be meant for the auditor's own staff.

When the check list is in question form, it is hardly different from a questionnaire. However, generally questionnaire is a popular medium for the evaluation of the internal control system.

The basic distinction between internal control questionnaire & check list are as under:
1. The ICQ incorporates a large number of detailed questions but the check list generally contains questions relating to the main control objective with the area under review.
2. In ICQ, questions are usually answered by company executives. However, in a check list, the same are required to be answered by auditor/auditor staff.
3. The significance of 'No' in an ICQ does indicate a weakness but the significance of that weakness is not revealed automatically. However, in the check list, a specific statement is required where an apparent weakness may prove to be material in relation to the accounts as a whole.

6.1.3 Flow chart

The flow charting technique can also be resorted to for evaluation of the internal control system. It is a graphic presentation of internal controls in the organisation and is normally drawn up to show the controls in each section or sub-section. As distinct from a narrative form, it provides the most concise and comprehensive way for reviewing the internal controls and the evaluator's findings. In a flow chart, narratives, though cannot perhaps be totally banished are reduced to the minimum and by that process, it can successfully bring the whole control structure, specially the essential parts thereof, in a condensed but wholly meaningful manner. It gives a bird's eye view of the system and is drawn up as a result of the auditor's review thereof. It should, however, not be understood that details are not reflected in a flow chart. Every detail relevant from the control point of view and the details about how an operation is performed can be included in the flow chart. Essentially a flow chart is a diagram full with lines and symbols and, if judicious use of them can be made, it is probably the most effective way of presenting the state of internal controls in the client's organisation.

A properly drawn up flow chart can provide a neat visual picture of the whole activities of the section or department involving flow of documents and activities. More specifically it can show-

(i) at what point a document is raised internally or received from external sources;

(ii) the number of copies in which a document is raised or received;

(iii) the intermediate stages set sequentially through which the document and the activity pass;

(iv) distribution of the documents to various sections, department or operations;

(v) checking authorisation and matching at relevant stages;

(vi) filing of the documents; and

(vii) final disposal by sending out or destruction.

As a matter of fact, a very sound knowledge of internal control requirements is imperative for, adopting flow-charting technique for evaluation of internal controls; also it demands a highly analytical mind to be able to see clearly the inter division of a job and the appropriate control at relevant points.

7. REPORTING TO CLIENTS ON INTERNAL CONTROL WEAKNESSES

The auditor should communicate such material weaknesses to the management or the audit committee, if any, on a timely basis. This communication should be, preferably, in writing through a letter of weakness or management letter. **Important points with regard to such a letter are as follows:**

(a) The letter lists down the area of weaknesses in the system and offers suggestions for improvement.

(b) It should clearly indicate that it discusses only weaknesses which have come to the attention of the auditor as a result of his audit and that his examination has not been designed to determine the adequacy of internal control for management.

(c) This letter serves as a valuable reference document for management for the purpose of revising the system and insisting on its strict implementation.

(d) The letter may also serve to minimize legal liability in the event of a major defalcation or other loss resulting from a weakness in internal control.

The practice of the issue of letter of weaknesses has a great merit in relieving the auditor from liability in case serious frauds or losses have occurred, which probably would not have taken place had the client taken due note of the auditor's points in the letter of weakness. In the case Re S.P. Catterson & Ltd. (1937, 81, Act L.R.62), the auditor was acquitted of the charge of negligence for employee's fraud in view of the fact that he had already informed the client about the unsatisfactory state in the specific areas of accounts and had suggested improvements which were not acted upon by the management.

The auditor shall also communicate to management at an appropriate level of responsibility on a timely basis:

(a) In writing, significant deficiencies in internal control that the auditor has communicated or intends to communicate to those charged with governance, unless it would be inappropriate to communicate directly to management in the circumstances; and

(b) Other deficiencies in internal control identified during the audit that have not been communicated to management by other parties and that, in the auditor's professional judgment, are of sufficient importance to merit.

The auditor shall include in the written communication of significant deficiencies in internal control:

(a)	A description of the deficiencies & an explanation of their potential effects; and
(b)	Sufficient information to enable those charged with governance and management to understand the context of the communication. In particular, the auditor shall explain that: a. The purpose of the audit was for the auditor to express an opinion on the financial statements; b. The audit included consideration of internal control relevant to the preparation of the financial statements 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 internal control; and c. The matters being reported are limited to those deficiencies that the auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to those charged with governance.

Based upon risks of material misstatements identified and assessed by the auditor, auditor develops responses to assessed risks.

SA 330, "The Auditor's Responses to Assessed Risks" *deals with the auditor's responsibility to design and implement responses to the risks of material misstatement identified and assessed by the auditor in accordance with SA 315.*

SA 330 states that:

- *The auditor shall design and implement overall responses to address the assessed risks of material misstatement at the financial statement level.*
- *The auditor shall design and perform further audit procedures whose nature, timing and extent are based on and are responsive to the assessed risks of material misstatement at the assertion level.*

In designing the further audit procedures to be performed, the auditor shall:
(a) Consider the reasons for the assessment given to the risk of mate misstatement at the assertion level for each class of transactions, account balance and disclosure, including:
(i) The likelihood of material misstatement due to the particular characteristics of the relevant class of transactions, account balance, or disclosure (i.e., the inherent risk); and *(ii) Whether the risk assessment takes into account the relevant controls (i.e., the control risk), thereby requiring the auditor to obtain audit evidence to determine whether the controls are operating effectively (i.e., the auditor intends to rely on the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures); and*
(b) Obtain more persuasive audit evidence the higher the auditor's assessment of risk.

The auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls when:

(a) The auditor's assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively (i.e., the auditor intends to rely on the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures); or

(b) Substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level.

8. FRAMEWORKS OF INTERNAL CONTROL

Guidance Note on Audit of Internal Financial Controls Over Financial Report: ICAI has issued a Guidance Note on Audit of Internal Financial Controls Over Financial Reporting which covers aspects such as Scope of reporting on internal financial controls under Companies Act 2013, essential components of internal controls, Technical guidance on audit of Internal Financial Controls, Implementation guidance on audit of Internal Financial Controls. The Guidance Note states as below:

"To state whether a set of financial statements presents a true and fair view, it is essential to benchmark and check the financial statements for compliance with the financial reporting framework.

The Accounting Standards specified under the Companies Act, 1956 (which are deemed to be applicable as per Section 133 of the 2013 Act, read with Rule 7 of Companies (Accounts) Rules, 2014) is one of the criteria constituting the financial reporting framework based on which companies prepare and present their financial statements and against which the auditors evaluate if the financial statements present a true and fair view of the state of affairs and operations of the company in an audit of the financial statements carried out under the Companies Act, 2013.

8.1 International Internal Control Frameworks

An overview of different internal control frameworks followed internationally are given below:

A. Internal Control- Integrated Framework issued by Committee of the Sponsoring Organisations of the Treadway Commission (COSO Framework)

COSO's Internal Control – Integrated Framework was introduced in 1992 as guidance on how to establish better controls so companies can achieve their objectives. COSO categorizes entity-level objectives into operations, financial reporting, and compliance. The framework includes more than 17 basic principles representing the fundamental concepts associated with its five components: control environment, risk assessment, control activities, information and communication, and monitoring. Some of the principles include key elements for compliance, such as integrity and ethical values, authorities and responsibilities, policies and procedures, and reporting deficiencies.

Here are the tiles of the 17 internal control principles by internal control component as presented in COSO's framework:

Control Environment	**Risk Assessment**	**Control Activities**	**Information and Communication**	**Monitoring**
Demonstrates commitment to integrity and ethical values	Specifies suitable objectives	Selects and develops control activities	Uses relevant information	Conducts ongoing and/or separate evaluations
Exercises oversight responsibility	Identifies and analyses risk	Selects and develops general controls over technology	Communicates internally	Evaluates and communicate deficiencies
EOstablishes structure, authority, and responsibility	Assesses fraud risk	Deploys through policies and procedures	Communicates externally	
Demonstrates commitment to competence	Identifies and analyses significant change			
Enforces accountability				

The COSO Framework is designed to be used by organizations to assess the effectiveness of the system of internal control to achieve objectives as determined by management. The Framework lists three categories of objectives as below:

- **Operations Objectives -** related to the effectiveness & efficiency of the entity's operations, including operational and financial performance goals, and safeguarding assets against loss.
- **Reporting Objectives -** related to internal and external financial and non-financial reporting to stakeholders, which would encompass reliability, timeliness, transparency, or other terms as established by regulators, standard setters, or the entity's policies.

- **Compliance objectives** - In the Framework, the compliance objective was described as "relating to the entity's compliance with applicable laws and regulations." The Framework considers the increased demands and complexities in laws, regulations, and accounting standards.

B. Guidance on Assessing Control published by the Canadian Institute of Chart Accountants (CoCo)

CoCo was introduced with the objective of improving organizational performance and decision- making with better controls, risk management, and corporate governance.

The **Criteria of Control (CoCo)** framework was developed by the Canadian Institute of Chartered Accountants with the objective of improving organisational performance and decision making with better controls, risk management, and corporate governance. The framework includes 20 criteria for effective control in four areas of an organization: purpose (direction), commitment (identity and values), capability (competence), and monitoring and learning (evolution).

The framework emphasizes that control involves the entire organization but begins on an individual level, with the employee.

The CoCo framework outlines criteria for effective control in the following four areas:

- Purpose
- Commitment
- Capability
- Monitoring and Learning

In order to assess whether controls exist and are operating effectively, each criterion would be examined to identify the controls that are in place to address them.

C. Control Objectives for Information and Related Technology (COBIT)

COBIT stands for Control Objectives for Information and Related Technology. It is a framework created by the ISACA (Information Systems Audit and Control Association) for IT governance and management. COBIT has 34 high-level processes that cover 210 control objectives categorized in four domains: planning and organization, acquisition and implementation, delivery and support, and monitoring and evaluation. It is designed as a supportive tool for managers and allows bridging the crucial gap between technical issues, business risks and control requirements.

Business managers are equipped with a model to deliver value to the organization and practice better risk management practices associated with the IT processes. It is a control model that guarantees the integrity of the information system. Today, COBIT is used globally by all managers who are responsible for the IT business processes. It is a thoroughly recognized guideline that can be applied to any organization across industries. Overall, COBIT ensures quality, control and reliability of information systems in organization, which is also the most important aspect of every modern business. This framework guides an organization on how to use IT resources (i.e., applications, information, infrastructure, and people) to manage IT domains, processes, and activities to respond to business requirements, which include compliance, effectiveness, efficiency, confidentiality, integrity, availability, and reliability. Well-governed IT practices can assist businesses in complying with laws, regulations, and contractual arrangements.

D. Internal Control: Guidance for Directors on the Combined Code, published by the Institute of Chartered Accountants in England & Wales (known as the Turn Report)

When the Combined Code of the Committee on Corporate Governance (the Code) was published, the Institute of Chartered Accountants in England & Wales agreed with the London Stock Exchange that it would provide guidance to assist listed companies to implement the requirements in the Code relating to internal control. The key principles of the Code are enunciated as below:

- The board should maintain a sound system of internal control to safeguard shareholders' investment and the company's assets.
- The directors should, at least annually, conduct a review of the effectiveness of the group's system of internal control and should report to shareholders that they have done so. The review should cover all controls, including financial, operational and compliance controls and risk management.

- Companies which do not have an internal audit function should from time to time review the need for one.

The guidance requires directors to exercise judgement in reviewing how the company has implemented the requirements of the Code relating to internal control and reporting to shareholders thereon. The guidance is based on the adoption by a company's board of a risk-based approach to establishing a sound system of internal control and reviewing its effectiveness. This should be incorporated by the company within its normal management and governance processes. It should not be treated as a separate exercise undertaken to meet regulatory requirements.

E. Sarbanes-Oxley Section 404

Section 404 of Sarbanes-Oxley Act (Sarbanes-Oxley Act Section 404) of United States of America mandates that all publicly-traded companies must establish internal controls and procedures for financial reporting and must document, test and maintain those controls and procedures to ensure their effectiveness. The purpose of SOX is to reduce the possibilities of corporate fraud by increasing the stringency of procedures and requirements for financial reporting. The Sarbanes Oxley Act, has revamped federal regulations pertaining to publicly traded companies' corporate governance and reporting obligations. It was followed up with constitution of PCAOB (Public Company Accounting Oversight Board). It regulates the audits of public companies and SEC-registered brokers and dealers in order to protect investors and further the public interest in the preparation of informative, accurate, and independent audit reports.

The SEC rules and PCAOB standard require that:

- Management perform a formal assessment of its controls over financial reporting including tests that confirm the design and operating effectiveness of the controls.
- Management include in its annual report an assessment of ICFR.
- The external auditors provide two opinions as part of a single integrated audit of the company:
  - An independent opinion on the effectiveness of the system of ICFR.
  - The traditional opinion on the financial statements.

5. AUDIT EVIDENCE

1. SA 500 AUDIT EVIDENCE

SA 500 deals with the auditor's responsibility to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion. It also explains what constitutes audit evidence in an audit of financial statements

❖ **Audit evidence** is the information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information.

SA 500 – "Audit Evidence"

1.1 Scope of the SA

- This SA deals with the auditor's responsibility to design and perform audit procedures to obtain sufficient and appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion.
- This SA is applicable to all the audit evidence obtained during the course of audit.

1.2 Objective of the auditor

- To design and perform audit procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base auditor's opinion.

1.3 Information to be used as audit evidence

- The auditor shall consider the relevance and reliability of the information to be used as audit evidence.
- When information from management expert is used, the auditor shall evaluate the competence, objectivity of the expert, appropriateness of the expert's work. When using information produced by the entity, the auditor shall evaluate the reliability, completeness, accuracy of the information.

1.4 Audit procedures to obtain audit evidence

- Audit evidence to draw reasonable conclusions on which to base the auditor's opinion is obtained by performing:

1. Risk Assessment procedures
2. Further audit procedures comprising of: Test of controls and Substantive procedures.

1.5 Inconsistency in or doubts over reliability of audit evidence

- The auditors shall determine what modifications or additions to audit procedures are necessary to resolve the matter and shall consider the effect of the matter, if any, on other aspects of the audit.

2. SA 501 AUDIT EVIDENCE - SPECIFIC CONSIDERATIONS FOR SELECTED ITEMS

2.1 Scope of the SA

This SA deals with specific considerations by the auditor in obtaining sufficient appropriate audit evidence with respect to inventory, litigation and claims and segment information in an audit of financial statements.

2.2 Objective of the auditor

To obtain sufficient and appropriate audit evidence regarding:

- Existence and condition of inventory
- Completeness of litigation and claims involving the entity.
- Presentation and disclosure of segment information in accordance with applicable FRF.

2.3 Inventory

a) If inventory is material, obtain evidence for existence and condition of inventory by:

1. Attence at physical inventory counting.
2. Performating audit procedures over the entity's final inventory records.

b) If inventory counting conducted at date other than the date of financial statements, perform additional procedures with respect to inventory between count date and date of financial statements.

c) If auditor is unable to attend the physical inventory counting due to unforsean circumstances, auditor to make/observe some physical count on alternate date and perform audit procedures on intervening transactions.

d) If attendance at inventory count is impracticable, auditor to perform alternate procedures. If it is not possible to do so, modify the opinion.

e) When inventory is under custody of third party, request confirmation from third party and perform inspection and other procedures.

2.4 Litigation and Claims

a) Auditor to perform audit procedures to identify litigation and claims by:

1. Inquiry of management.
2. Reviewing minutes of meetings.
3. Reviewing legal expense accounts

b) If auditor assesses risk of material misstatement, seek direct communication with entity's external legal counsel.

c) If auditor is unable to communicate with the external legal counsel, modify the opinion as per SA 705.

d) Obtain Written Representation that all know actual or possible litigation and claims have been disclosed to the auditor and appropriately accounted for as per applicable FRF.

2.5 Segment Information

Auditor to obtain audit evidence regarding presentation and disclosure of segment information in accordance with applicable FRF by:

1. Understanding the methods used by the management in determine segment information
2. Performating analytical procedures.

3. SA 505 EXTERNAL CONFIRMATIONS

3.1 Scope of the SA & Objective of the auditor

- **Scope:** This SA deals with auditor's use of external confirmation procedures to obtain audit evidence.
- **Objective:** To design and perform external confirmation procedures to obtain relevant and reliable audit evidence.

3.2 External Confirmation Procedures

- Determining the information to be confirmed/requested.
- Selecting the appropriate confirming party.
- Designing the confirmation requests.
- Sending the requests, including follow-up requests.

3.3 Management's refusal to allow the audit to send a confirmation request

- Inquire as to management's reasons for the refusal, and seek audit evidence as to their validity and reasonableness.
- Evaluate the implications of management's refusal on the auditor's assessment of the relevant risks of material misstatement, including the risk of fraud, and on the nature, timing and extent of other audit procedures, and
- Perform alternative audit procedures designed to obtain relevant and reliable audit evidence.
- If management's refusal is unreasonable, then communicate with TCWG and consider the implications on audit and auditor's opinion.

3.4 Results of the External Confirmation procedures

A) Reliability of responses to confirmation requests: If auditor has doubt about reliability of response, auditor to obtain further audit evidence. If auditor determiners response is not reliable, auditor to evaluate the implications on the assessment of risk of material misstatement.

B) Non Response: Auditor shall perform alternative audit procedures.

C) When a response to positive confirmation is necessary and the same is not received: Determine the implications on the audit and the auditors opinion.

D) Exception: Auditor shall investigate exceptions to determine whether or not they are indicative of misstatement.

E) Negative confirmation: Auditor to use negative confirmation as sole substantive audit procedures when:

1. Assessed Risk of Material misstatement is low and relevant controls are effective.
2. The population comprise of large number of small, homogeneous transactions.

3. A very low exception rate is expected.

4. The auditor is not aware of circumstances that would cause recipients of negative confirmation requests to disregard such requests.

4. SA 510 INITIAL AUDIT ENGAGEMENTS - OPENING BALANCES

4.1 Scope of the SA and Objective of SA

To obtain sufficient appropriate audit evidence about:

1. Whether opening balances contain misstatements that materially affect the current period's financial statements.
2. Whether appropriate accounting policies are consistently applied and any changes where to has been properly accounted for presented and disclosed.

4.2 Audit Procedures

♦ **The auditor shall:**

1. Read the most recent financial statements and predecessor's auditor's report.
2. Determine whether prior period's closing balance has been correctly brought forward.
3. Determine whether the opening balances reflect appropriate accounting policies.
4. Perform audit procedures on opening balances.
5. If current period financial statements are misstated due to misstatement in opening balances, communicate with management or TCWG.

♦ **Consistency of Accounting Policies:**

Obtain audit evidence as to whether the accounting policies are consistently applied and in case of any changes, whether properly accounted for, presented and disclosed.

♦ **Relevant Information in the Predecessor's Auditor's Report:**

1. If modification in predecessor auditor's report, evaluate the effect of the matter giving rise to such modification with respect to current period's financial statements.

4.3 Audit Conclusion and reporting

♦ Opening Balances:

1. If audit is unable to obtain audit evidence regarding opening balances - Qualified /disclaimer of opinion.

2. If auditor condudes opening balances contain misstatement, not properly presented/disclosed - Qualified / Adverse Opinion.

- **Consistency of Accounting Policies:**

  If auditor concludes that accounting policies are not consistently applied in relation to opening balances or changes are not properly accounted for - Qualified/Adverse Opinion.

- **Modification to the opinion in the predecessor's auditor's report:**

  If the modication is relevant and material to the current period's financial statements, auditor shall modify the current period audit report.

5. SA 530 AUDIT SAMPLING

SA 530 deals with the auditor's use of statistical and non-statistical sampling when designing and selecting the audit sample, performing tests of controls and tests of details and evaluating the results from the sample.

Definition

Audit Sampling

The application of audit procedures to less than 100% of items within a population of audit relevance such that all the sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population.

5.1 Scope of the SA & Objective of the auditor

- **Scope:** This SA applies when the auditor has decided to use audit sampling in performing audit procedures. It deals with auditor's use of statistical and non-statistical sampling.
- **Objective:** To provide a reasonable basis for the auditor to draw conclusions about the population from which the sample is selected.

5.2 Sample design, size and selection of items for testing

1. While designing audit sample, the auditor shall consider the purpose of the audit procedure and the characteristics of the population.

2. The auditor shall determine sample size sufficient to reduce sampling risk to an acceptably low level.

3. The auditor shall select items for the sample such that each sampling unit in the population has a chance of selection.

5.3 Performing Audit Procedures

1. The auditor shall perform appropriate audit procedure on each item selected.
2. If audit procedure is not applicable on the selected item, apply the procedure on a replacement item.
3. If the auditor is unable to apply the designed audit procedure to a selected item, treat that item as a deviation from the prescribed control, in case of tests of controls, or a misstatement, in the case of tests of details.

5.4 Other points of consideration

1. The auditor shall investigate the nature and cause of deviation or misstatement identified and evaluate its possible effect.
2. When a deviation/misstatement is considered as anomaly, the auditor shall perform audit procedures to obtain high degree of certainty that it is not representative of the population.
3. For test of details, the auditor shall project misstatements found in the sample to the population.
4. The auditor shall evaluate the results of the sample and whether the use of audit sampling has provided a reasonable basis for conclusion about the population tested.

6. SA 550 RELATED PARTIES

SA 550 deals with the auditor's responsibilities regarding related party relationships and transactions when performing an audit of financial statements. Specifically, it applies in relation to risks of material misstatement associated with related party relationships and transactions.

6.1 Scope of the SA

- This SA deals with the auditor's responsibilities regarding related party relationships and transactions. It expands on how SA 315, SA 330, SA 240 are to be applied in relation to related party relationships and transactions.

6.2 Objectives of the auditor

- To obtain an understanding of the related party transactions to:

1. recognize fraud risk factors arising from such transactions.
2. conclude whether financial statements in so far as they are effected by such transactions

a) achieve a true and fair presentation.

b) are not misleading.

- To obtain audit evidence as to whether the related party transactions are properly identified, accounted for, and disclosed in the financial statements.

6.3 Requirements of the SA

1. Risk Assessment procedures and related activities.
2. Understanding the Entity's related party relationships and transactions.
3. Maintaining alertness for related party information when reviewing records or documents.
4. Sharing related party information with the Engagement team.
5. Identification and assessment of the risk of material misstatement associated with related party transactions and relationships.
6. Responses to the Risks of Material Misstatement associated with related party relationships and transactions.

6.4 Identification of previously unidentified or undisclosed related part transactions.

1. Auditor shall determine whether the underlying circumstances confirm the existence of such transactions.
2. Communicate within the team.
3. Request management to identify all transactions with newly identified related parties.
4. Perform more substantive procedures.
5. Reconsider risks with respect to other related parties.
6. If non-disclosure by the management appears intentional, evaluate the implications for the audit.

6.5 Identified significant related party transactions outside the entity's normal course of business

1. Inspect the underlying contracts and evaluate:

a) the business rationale of the transactions.

b) whether the terms of transactions are consistent with management's explanations.

c) whether such transactions have been properly accounted for.

2. Obtain audit evidence that the transactions have been appropriately authorised and approved.

6.6 Other important points

♦ **The auditor shall obtain Written Representation that:**

a) all the related parties and related party transactions have been disclosed to the auditor and

b) all such transactions have been properly accounted for and disclosed.

♦ **Communication with TCWG**

The auditor shall communicate with TCWG significant matters arising during the audit in connection with the entity's related parties.

♦ **Documentation:**

The auditor shall include in audit documentation names of the related parties and the nature of the related party transactions.

6. COMPLETION AND REVIEW

1. SA 560 SUBSEQUENT EVENTS

SA 560 deals with the auditor's responsibilities relating to subsequent events in an audit of financial statements. The objectives of auditor in this regard are to obtain sufficient appropriate evidence about whether such events are appropriately adjusted or disclosed in financial statements. Further, in case some facts have come to his knowledge after date of auditor's report, to respond to those facts such that had they been known to him at the date of the report, they may have caused him to amend the auditor's report.

1.1 Scope of the SA

This SA deals with auditor's responsibilities relating to subsequent events in an audit of financial statements.

1.2 Definitions

Subsequent Events:

Events occurring between the date of the financial statements and the date of the auditor's report, and facts that become known to the auditor after the date of the auditor's report.

1.3 Objectives of the auditor

- Obtain sufficient appropriate audit evidence about whether events occurring between the date of the financial statements and the date of the auditor's report that require adjustment of, or disclosure in, the financial statements are appropriately reflected in those financial statements.
- Respond appropriately to the facts that become known to the auditor after the date of the auditor's report, that, had they been known to the auditor at that date, may have caused the auditor to amend the auditor's report.

1.4 Events occurring between the date of the Financial Statements and date of the auditor's report

1. The auditor shall perform audit procedures to ensure that all such events have been

identified.

2. The auditor shall consider the auditor's risk assessment in determining the nature and extent of such procedures.

3. If such event is identified, determine whether such event is appropriately reflected in financial statements.

4. Obtain Written Representation that all such events have been adjusted or disclosed.

1.5 Facts which become known to the auditor after the date of the auditor's report but before the date the financial statements are issued

1. Discuss the matter with management or TCWG.

2. Determine whether the financial statements need amendment\

3. Inquire how management intends to address the matter in the financial statements.

4.1 If management amends the financial statements, auditor should extend the audit procedures and

1. Either amend the audit report to include an additional date restricted to the amendment.

2. Or provide a new/amended report including a statement in EOM/OM para.

4.2 If management doesn't amend the financial statements.

1. If audit report not yet provided to the management, modify the opinion.

2. If audit report has already been provided to the management, notify TCWG not to issue it to third parties. If still issued then take appropriate action to prevent reliance on the auditor's report.

1.6 Facts that become known to the auditor after the financial statements have been issued

1. Discuss the matter with management or TCWG.

2. Determine whether the financial statements need amendment.

3. Inquire how management intends to address the matter in the financial statements.

4. **Review if management has taken steps to inform about the situation to everyone in receipt of the previously issued financial statements.**

1. If steps taken, issue new/amended report with EOM/OM para.
2. If steps not taken, then take appreopriate steps to prevent reliance on the auditor's report.

2. SA 570 GOING CONCERN

SA 570 Going Concern deals with the auditor's responsibilities in the audit of financial statements relating to going concern and the implications for the auditor's report.

The auditor's responsibilities are to obtain sufficient appropriate audit evidence regarding use of the going concern basis of accounting in the preparation of the financial statements by the management. On the basis of evidence obtained, it is concluded whether a material uncertainty exists relating to events or conditions that may cast a significant doubt on the entity's ability to continue as a going concern.

2.1 Scope of the SA

This SA deals with the auditor's responsibilities in the audit of financial statements relating to going concern and the implications on the auditor's report.

2.2 Responsibilities of the management

1. To make specific assessment of the entity's ability to continue as a going concern.
2. To make appropriate disclosures in connection with going concern in the financial statements.

2.3 Responsibilities of the auditor

1. To obtain sufficient and appropriate audit evidence and conclude on the appropriateness of the management's use of going concern.
2. To assess whether a material uncertainty exists about the entity's ability to continue as a going concern.
3. However, auditor cannot be expected to guarantee the entity's ability to continue as a going concern.

2.4	***When conditions or events are identified***
1.	*Requesting management to make its assessment relating to entity's ability to continue as a going concern.*
2.	*Evaluating management's plan of future actions.*
3.	*Analysing the cash flow forecast of the entity.*
4.	*Considering the additional facts or information available.*
5.	*Requesting Written Representation from management regarding the plans of future actions and the feasibility of these plans.*
2.5	***Implications on the auditor's report***
1	*Use of Going Concern Basis of Accounting is in appropriate. The auditor shall express an adverse opinion.*
2	*Use of Going Concern basis of accounting is appropriate but a material uncertainty exists and:*
3	*Adequate disclosure of material uncertainty is made in the financial statements. Unmodified Opinion and a separate section "Material Uncertainty related to going concern".*
4	*Management unwilling to make or extend its assessment-Auditor shall consider the implications for the auditor's report.*
2.6	***Other Important Points to be considered***
♦	*The auditor shall communicate with TCWG, events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern.*
♦	*If there is delay in the approval of the financial statements and the auditor believes that such delay can be related to events or conditions relating to going concern assessment, the auditor shall perform additional procedures as well as consider the effect on auditor's conclusion.*
♦	*Use of Going Concern basis of accounting is appropriate but a material uncertainty exists and; Adequate disclosure of material uncertainty is not made in the financial statements – Qualified/adverse opinion and mention in the basis of opinion paragraph.*

3. SA 580 WRITTEN REPRESENTATIONS

SA 580 Written representations deals with the auditor's responsibility to obtain written representations from management and, where appropriate, those charged with governance. Although written representations provide **necessary audit evidence**, they **do not** provide **sufficient appropriate audit evidence** on their own about any of the matters with which they deal. Furthermore, the fact that management has provided reliable written representations does not affect the nature or extent of other audit evidence that the auditor obtains about the fulfilment of management's responsibilities or about specific assertions.

3.1 Scope of the SA

- This SA deals with the auditor's responsibility to obtain written representation from management and, where appropriate, those charged with governance.

3.2 Objectives of the auditor

1. To obtain written representation from the management or TCWG that they believe that they have fulfilled their responsibility for the preparation of the financial statements and for the completeness of the information provided to the auditor.
2. To support other audit evidence relevant to the financial statements or specific assertions in the financial statements by means of written representations.
3. To respond appropriately to written representation provided by management/TCWG.

3.3 Written Representation as Audit Evidence

- Although Written Representations provide necessary audit evidence, they do not provide sufficient appropriate audit evidence on their own.

3.4 Date & Periods covered by Written Representation

- The date of Written Representation shall be as near as practicable to, but not after, the date of the auditor's report on the financial statements.
- Written Representation shall be for all financial statements and periods referred to in the auditor's report.

3.5 Important points to be considered

- **Doubts as to reliability of Written Representations:**
  - If written representations are inconsistent with other audit evidence, audit shall perform audit procedures to resolve the matter.
  - If the auditor concludes that the written representation are not reliable, the auditor shall take appropriate action in accordance with SA 705.

- **Requested Written Representation not provided:**

  Auditor shall discuss with the management, re-evaluate the integrity of management, take appropriate actions including the impact on audit report as per SA 705.

7. REPORTING

1. INTRODUCTION

Assuming you are an auditor and have concluded the audit field work, your next step will be issuance of the audit report. Issuance of Audit report is the culmination of the Audit Work. It is the most important deliverable for a Statutory Auditor.

2. THE AUDITOR'S REPORT ON FINANCIAL STATEMENTS

The SA 700 series is purely dedicated to the auditor's report to be issued by the auditor. There are following SAs which you need to be aware of:

Particulars	Head
SA-700	Forming an Opinion and Reporting on Financial Statements
SA-701	Communicating Key Audit Matters in the Independent Auditor's Report
SA-705	Modifications to the Opinion in the Independent Auditor's Report
SA-706	Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report

3. SA-700, "FORMING AN OPINION AND REPORTING ON THE FINANCIAL STATEMENTS"

Objective: As per SA 700 the objectives of the auditor are:

(a) To form an opinion on the financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained; and

(b) To express clearly that opinion through a written report.

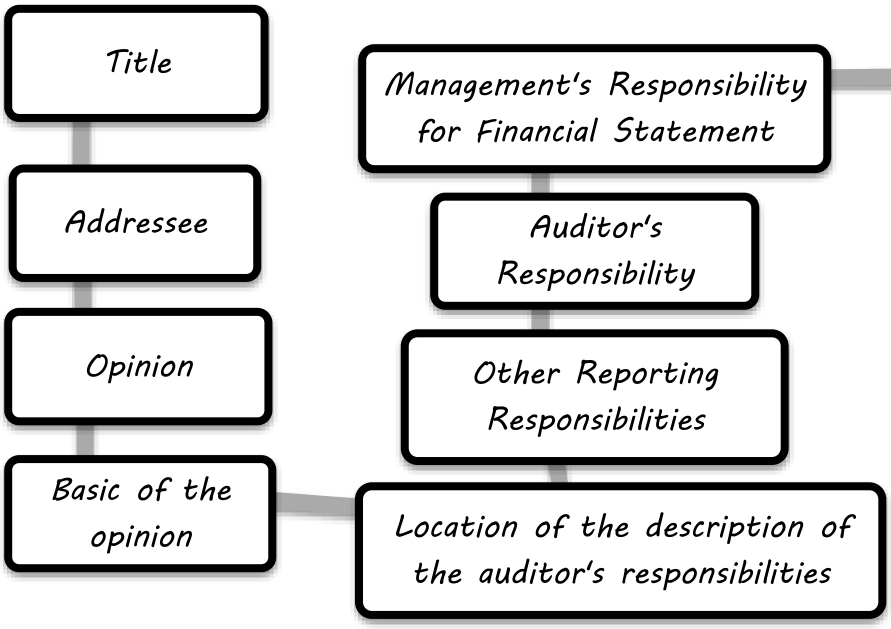
3.1 Purpose

Forming an opinion on the Financial Statements

The auditor shall form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework. In order to form that opinion, the auditor shall obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement whether due to fraud or error. Further, when the financial statements are prepared in accordance with a fair presentation framework, the auditor shall also evaluate as to whether the financial statements achieve fair presentation by considering:

1. The overall presentation, structure & content of the financial statements; and
2. Whether the financial statements, including the related notes, represent the underlying transactions and events in a manner that achieves fair presentation.

3.2 Basic Elements of the Auditor's Report



1. **Title:** The auditor's report shall have a title that clearly indicates that it is the report of an independent auditor.

2. **Addressee:** The auditor's report shall be addressed as required by the circumstances of the engagement.

3. **Auditor's Opinion:** The first section of the auditor's report shall include the auditor's opinion, and shall have the heading "Opinion."

The Opinion section of the auditor's report shall also:

(a) Identify the entity whose financial statements have been audited;

(b) State that the financial statements have been audited;

(c) Identify the title of each statement comprising the financial statements;

(d) Refer to the notes, including the summary of significant accounting policies; and

(e) Specify the date of, or period covered by, each financial statement comprising the financial statements.

When expressing an unmodified opinion on financial statements prepared in accordance with a fair presentation framework, the auditor's opinion shall, unless otherwise required by law or regulation, use one of the following phrases, which are regarded as being equivalent:

(i) In our opinion, the accompanying financial statements present fairly, in all material respects, [...] in accordance with [the applicable financial reporting framework]; or

(ii) In our opinion, the accompanying financial statements give a true and fair view of [...] in accordance with [the applicable financial reporting framework].

When expressing an unmodified opinion on financial statements prepared in accordance with a compliance framework, the auditor's opinion shall be that the accompanying financial statements are prepared, in all material respects, in accordance with [the applicable financial reporting framework].

4. **Basis for Opinion:** The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion", that:

(a) States that the audit was conducted in accordance with Standards on Auditing;
(b) Refers to the section of the auditor's report that describes the auditor's responsibilities under the SAs;
(c) Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall refer to the Code of Ethics issued by ICAI
(d) States whether the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's opinion.

5. **Going Concern:** Where applicable, the auditor shall report in accordance with SA 570. SA 570 deals with the auditor's responsibilities in the audit of financial statements relating to going concern and the implications for the auditor's report.

I. **Use of Going Concern Basis of Accounting Is Inappropriate:** If the financial statements have been prepared using the going concern basis of accounting but, in the auditor's judgment, management's use of the going concern basis of accounting in the preparation of the financial statements is inappropriate, the auditor shall express an adverse opinion.

II. **Use of Going Concern Basis of Accounting Is Appropriate but a Material Uncertainty Exists and:**

(A) **Adequate Disclosure of a Material Uncertainty Is Made in the Financial Statements:** If adequate disclosure about the material uncertainty is made in the financial statements, the auditor shall express an unmodified opinion & the auditor's report shall include a separate section under the heading "Material Uncertainty Related to Going Concern" to:

(i) Draw attention to the note in the financial statements that discloses the matters

(ii) State that these events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the auditor's opinion is not modified in respect of the matter.

(B) **Adequate Disclosure of a Material Uncertainty Is Not Made in the Financial Statements:** If adequate disclosure about the material uncertainty is not made in the financial statements, the auditor shall:

(i) Express a qualified opinion or adverse opinion, as appropriate, in accordance with SA 705 (Revised); and

(ii) In the Basis for Qualified (Adverse) Opinion section of the auditor's report, state that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not adequately disclose this matter.

(C) **Management Unwilling to Make or Extend Its Assessment:** If management is unwilling to make or extend its assessment when requested to do so by the auditor, the auditor shall consider the implications for the auditor's report.

6. **Key Audit Matters:** For audits of complete sets of general purpose financial statements

of listed entities, the auditor shall communicate key audit matters in the auditor's report in accordance with SA 701.

7. Responsibilities for the Financial Statements:

This section of the auditor's report shall describe management's responsibility for:

(a) Preparing the financial statements in accordance with the applicable financial reporting framework, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and

(b) Assessing the entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern. The explanation of management's responsibility for this assessment shall include a description of when the use of the going concern basis of accounting is appropriate.

8. Auditor's Responsibilities for the Audit of the Financial Statements:

(I) This section of the auditor's report shall:

(a) State that the objectives of the auditor are to:

(i) Obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error; and

(ii) Issue an auditor's report that includes the auditor's opinion

(b) State that reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SAs will always detect a material misstatement when it exists; and

(c) State that misstatements can arise from fraud or error, and either:

(i) Describe that they are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements; or

(ii) Provide a definition or description of materiality in accordance with the applicable financial reporting framework.

(II) The Auditor's Responsibilities for the Audit of the Financial Statements section of the auditor's report shall further:

Auditor's Responsibilities in Audit of FS

- To exercises professional judgement & maintains professional skepticism throughout the audit as per SAs:
- To describe an audit by stating that the auditor's responsibilities are:
  - To identify and assess the risks of material misstatement of the FS
  - To obtain an understanding of internal control relevant for audit to design audit procedures
  - To evaluate the appropriateness of:
    - Accounting policies used
    - Reasonableness of accounting estimates
    - Related disclosures made by management
  - To conclude on the appropriateness of management's use of the going concern
  - to evaluate the overall presentation, structure and content of the financial statements
- To describe the auditor's responsibilities in a group audit engagement as per SA 600

(III) The Auditor's Responsibilities for the Audit of the Financial Statements section of the auditor's report also shall:

(a) **State that the auditor communicates with those charged with governance regarding, among other matters:**

- ◈ the planned scope and timing of the audit and
- ◈ significant audit findings,
- ◈ including any significant deficiencies in internal control that the auditor identifies during the audit;

(b) **State that the auditor provides those charged with governance with a statement that the auditor has:**

- complied with relevant ethical requirements regarding independence and
- communicate with them all relationships and
- other matters that may reasonably be thought to bear on the auditor's independence, and where applicable, related safeguards; and

(c) For audits of financial statements of all such entities **for which key audit matters are communicated in accordance with SA 701,** state that, from the matters communicated with those charged with governance, the auditor determines those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters.

9. **Location of the description of the auditor's responsibilities for the audit of the financial statements:** The description of the auditor's responsibilities for the audit of the financial statements required by this SA shall be included:

(a) Within the body of the auditor's report;

(b) Within an appendix to the auditor's report, in which case the auditor's report shall include a reference to the location of the appendix; or

(c) By a specific reference within the auditor's report to the location of such a description on a website of an appropriate authority, where law, regulation or the auditing standards expressly permit the auditor to do so.

10. **Other Reporting Responsibilities:**

(a) If the auditor addresses other reporting responsibilities in the auditor's report on the financial statements that are in addition to the auditor's responsibilities under the SAs, these other reporting responsibilities shall be addressed in a separate section in the auditor's report with a heading titled "Report on Other Legal and Regulatory Requirements" or otherwise as appropriate to the content of the section, unless these other reporting responsibilities address the same topics as those presented under the reporting responsibilities required by the SAs in which case the other reporting responsibilities may be presented in the same section as the related report elements required by the SAs.

(b) If other reporting responsibilities are presented in the same section as the related report elements required by the SAs, the auditor's report shall clearly differentiate the other reporting responsibilities from the reporting that is required by the SAs.

(c) If the auditor's report contains a separate section that addresses other reporting responsibilities, the requirements of this SA shall be included under a section with a heading "Report on the Audit of the Financial Statements." The "Report on Other Legal and Regulatory Requirements" shall follow the "Report on the Audit of the Financial Statements."

11. **Signature of the Auditor:** The auditor's report shall be signed. The report is signed by the auditor (i.e. the engagement partner) in his personal name. Where the firm is appointed as the auditor, the report is signed in the personal name of the auditor and in the name of the audit firm. The partner/proprietor signing the audit report also needs to mention the membership number assigned by the Institute of Chartered Accountants of India. They also include the registration number of the firm, wherever applicable, as allotted by ICAI, in the audit reports signed by them.

12. **Place of Signature:** The auditor's report shall name specific location, which is ordinarily the city where the audit report is signed.

13. **Date of the Auditor's Report:** The auditor's report shall be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements, including evidence that:

- All the statements that comprise the financial statements, including the related notes, have been prepared; and
- Those with the recognized authority have asserted that they have taken responsibility for those financial statements.

3.3 Auditor's Report Prescribed by Law or Regulation

(1) A title.

(2) An addressee, as required by the circumstances of the engagement.

(3) An Opinion section containing an expression of opinion on the financial statements and

a reference to the applicable financial reporting framework used to prepare the financial statements.

(4) An identification of the entity's financial statements that have been audited.

(5) A statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall refer to the Code of Ethics issued by ICAI.

(6) Where applicable, a section that addresses, and is not inconsistent with, the reporting requirements of SA 570.

(7) Where applicable, a Basis for Qualified (or Adverse) Opinion section that addresses, and is not inconsistent with, the reporting requirements of SA 570 (Revised).

(8) Where applicable, a section that includes the information required by SA 701, or additional information about the audit that is prescribed by law or regulation and that addresses, and is not inconsistent with, the reporting requirements in that SA 701.

(9) A description of management's responsibilities for the preparation of the financial statements and an identification of those responsible for the oversight of the financial reporting process that addresses, and is not inconsistent with, the requirements.

(10) A reference to Standards on Auditing and the law or regulation, and a description of the auditor's responsibilities for an audit of the financial statements that addresses, and is not inconsistent with, the requirements.

(11) The auditor's signature.

(12) The Place of signature

(13) The date of the auditor's report.

Students may note that the Chartered Accountants need to ensure compliance with all the requirements relating to signature prescribed in the relevant law or regulation, SAs and relevant announcements/ clarifications issued by ICAI on the matter including the requirement to mention UDIN (mandatory from 1stJuly 2019) (UDIN - UNIQUE DOCUMENT IDENTIFICATION NUMBER.)The requirement to mention UDIN is applicable both for manually and digitally signed reports/certificates including certificates uploaded online.

3.4 Auditor's Report for Audits Conducted in Accordance with Both Standards on Auditing Issued by ICAI and International Standards on Auditing or Auditing Standards of Any Other Jurisdiction:

If this is the case, the auditor's report may refer to Standards on Auditing in addition to the International Standards on Auditing or auditing standards of such other jurisdiction, but the auditor shall do so only if:

(a) There is no conflict between the requirements in the ISAs or such auditing standards of other jurisdiction and those in SAs that would lead the auditor:

(i) to form a different opinion, or

(ii) not to include an Emphasis of Matter paragraph or Other Matter paragraph that, in the particular circumstances, is required by SAs; and

(b) The auditor's report includes, at a minimum, each of the elements set out in Auditor's Report Prescribed by Law or Regulation discussed above when the auditor uses the layout or wording specified by the Standards on Auditing. However, reference to "law or regulation" in above paragraph shall be read as reference to the Standards on Auditing. The auditor's report shall thereby identify such Standards on Auditing.

3.5 Supplementary Information Presented with the Financial Statements

If supplementary information that is not required by the applicable financial reporting framework is:	
presented with the audited financial statements, the auditor shall evaluate whether, in the auditor's professional judgment, supplementary information is nevertheless an integral part of the financial statements due to its nature or how it is presented. When it is an integral part of the financial statements, the supplementary information shall be covered by the auditor's opinion.	not considered an integral part of the audited financial statements, the auditor shall evaluate whether such supplementary information is presented in a way that sufficiently and clearly differentiates it from the audited financial statements. If this is not the case, then the auditor shall ask management to change how the unaudited supplementary information is presented. If management refuses to do so, the auditor shall identify the unaudited supplementary information and explain in the auditor's report that such supplementary information has not been audited.

4. SA 701 COMMUNICATING KEY AUDIT MATTERS INTHE INDEPENDENT AUDITOR'S REPORT

4.1 Purpose

The purpose of communicating key audit matters is to enhance the communicative value of the auditor's report by providing greater transparency about the audit that was performed.

Objective

- To enhance the communicative value of the auditor's report by providing greater transparency about the audit that was performed.
- To assist the user in understanding those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period.

4.2 Scope

Communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor's report is not:

(a) A substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation;

(b) A substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with SA 705 (Revised);

(c) A substitute for reporting in accordance with SA 570 (Revised) when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern; or

(d) A separate opinion on individual matters.

❖ Applicability of SA 701

♦ This SA applies to audits of complete sets of general purpose financial statements of:

- listed entities and

- circumstances when the auditor otherwise decides to communicate key audit matters in the auditor's report and
- required by law or regulation to communicate key audit matters in the auditor's report.

However, SA 705 (Revised) prohibits the auditor from communicating key audit matters when the auditor disclaims an opinion on the financial statements, unless such reporting is required by law or regulation.

4.3 Determining Key Audit Matters

The auditor shall determine, from the matters communicated with those charged with governance, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor shall take into account the following:

(a) Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with SA 315

(b) Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.

(c) The effect on the audit of significant events or transactions that occurred during the period.

Examples of Key Audit Matters:

- Assessment of Impairment,
- Provision for losses and contingencies,
- Valuation of financial instruments,
- Matters relating to Revenue recognition,
- Taxation matters (multiple tax jurisdictions, uncertain tax position, deferred tax assets).

4.4 Communicating Key Audit Matters

The introductory language in this section of the auditor's report shall state that:

(a) Key audit matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements [of the current period]; and.

(b) These matters were addressed in the context of the audit of the financial statements as a whole, and in forming the auditor's opinion thereon, and the auditor does not provide a separate opinion on these matters.

In case there are no Key Audit Matter to communicate, the auditors' report must specifically mention that by carrying a Key Audit Matter Paragraph and under which they shall mention that there are no Key Audit matter to communicate.

5. SA 705, "MODIFICATIONS TO THE OPINION IN THE INDEPENDENT AUDITOR'S REPORT"

5.1 Types of Modified Opinions:

Types of Modified Opinions as per SA 705:	(i) Qualified Opinion
	(ii) Adverse Opinion
	(iii) Disclaimer of Opinion

The decision regarding which type of modified opinion is appropriate depends upon:

(a) The nature of the matter giving rise to the modification, that is, whether the financial statements are materially misstated or, in the case of an inability to obtain sufficient appropriate audit evidence, may be materially misstated; and

(b) The auditor's judgment about the pervasiveness of the effects or possible effects of the matter on the financial statements.

5.2 Objective

The objective of the auditor is to express clearly an appropriately modified opinion on the financial statements that is necessary when:

(a) The auditor concludes, based on the audit evidence obtained, that the financial statements as a whole are not free from material misstatement; or

(b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

5.3 Circumstances When a Modification to the Auditor's Opinion is Required:

The auditor shall modify the opinion in the auditor's report when:

The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or	The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

5.4 Determining the Type of Modification to the Auditor's Opinion:

5.4.1 **Qualified Opinion:** The auditor shall express a qualified opinion when:

(a) The auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or

(b) The auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive

5.4.2 **Adverse Opinion:** The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

5.4.3 **Disclaimer of Opinion:** The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive. The auditor shall disclaim an opinion when, in extremely rare circumstances involving multiple uncertainties, the auditor concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.

5.4.4 **What is Pervasive:** Pervasive is a term used in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence.

Pervasive effects on the financial statements are those that in the auditor's judgment:

1. Are not confined to specific elements, accounts or items of the financial statements;

2. If so confined, represent or could represent a substantial proportion of the financial statements; or

3. In relation to disclosures, are fundamental to users' understanding of the financial statements.

Pervasive, therefore, is that which is not localised to any one or two elements of a financial statements, but the impact is across various elements of the financial statements.

5.5 Consequence of an Inability to Obtain Sufficient Appropriate Audit Evidence Due to a Management-Imposed Limitation after the Auditor Has Accepted the Engagement

If, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the scope of the audit that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor shall request that management remove the limitation.

If management refuses to remove the limitation, the auditor shall communicate the matter to those charged with governance, unless all of those charged with governance are involved in managing the entity, and determine whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence.

5.5.1 If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall determine the implications as follows:

(a) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive, the auditor shall qualify the opinion; or

(b) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, the auditor shall:

(i) Withdraw from the audit, where practicable & possible under applicable law or regulation; or

(ii) If withdrawal from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial statements.

5.6 If the auditor decides to withdraw

When the auditor decides to withdraw before withdrawing, the auditor shall communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion.

5.6.1 **Where Auditors' withdrawal is not permitted:** The listing agreement and the Securities and Exchange Board of India's directive on the resignation of auditor does not permit withdrawing from the engagement without issuing the audit / review report. The said directive contained in circular no. CIR/CFD/CMD1/114/2019 dated October 18, 2019 issued by the Securities and Exchange Board of India inter-alia provides that

If the auditor proposes to resign:

a) within 45 days from the end of any of the quarters of a period covered under the appointment, then the auditor shall, before such resignation, issue the audit / limited review report for such quarter.

b) after 45 days from the end any of the quarters of a period covered under the appointment, then we shall, before such resignation, issue the audit / Limited review report for such quarter as well as the next quarter.

c) If the Limited review report has been issued for all the three quarters, then the auditor shall issue the audit report for the full year before resigning from the engagement.

ICAI announcement on the Resignation of Audit: The ICAI has made an announcement that the auditor of an unlisted company shall not mention "professional pre- occupation" as a reason for the resignation. The auditor shall mention the reasons clearly for the resignation in the resignation letter issued to the Company.

5.7. Other Considerations Relating to an Adverse Opinion or Disclaimer of Opinion

When the auditor considers it necessary to express an adverse opinion or disclaim an opinion on the financial statements as a whole, the auditor's report <u>shall not</u> also include an unmodified opinion with respect to the same financial reporting framework on a single financial statement or one or more specific elements, accounts or items of a financial statement. To include such an unmodified opinion in the same report in these circumstances would contradict the auditor's adverse opinion or disclaimer of opinion on the financial statements as a whole.

5.8 Form and Content of the Auditor's Report When the Opinion is Modified

When the auditor modifies the audit opinion, the auditor shall use the heading "Qualified Opinion," "Adverse Opinion," or "Disclaimer of Opinion," as appropriate, for the Opinion section.

5.8.1 What special consideration are required for expressing Qualified Opinion?

When the auditor expresses a qualified opinion due to a material misstatement in the financial statements, the auditor shall state that, in the auditor's opinion, except for the effects of the matter(s) described in the Basis for Qualified Opinion section:

(a) When reporting in accordance with a fair presentation framework, the accompanying financial statements present fairly, in all material respects (or give a true and fair view of) [...] in accordance with [the applicable financial reporting framework]; or

(b) When reporting in accordance with a compliance framework, the accompanying financial statements have been prepared, in all material respects, in accordance with [the applicable financial reporting framework].

When the modification arises from an inability to obtain sufficient appropriate audit evidence, the auditor shall use the corresponding phrase "except for the possible effects of the matter(s) …" for the modified opinion.

5.8.2 What special consideration needed or expressing Adverse Opinion?

When the auditor expresses an adverse opinion, the auditor shall state that, in the auditor's opinion, because of the significance of the matter(s) described in the Basis for Adverse Opinion section:

(a) When reporting in accordance with a fair presentation framework, the accompanying financial statements do not present fairly (or give a true and fair view of) [...] in accordance with [the applicable financial reporting framework]; or

(b) When reporting in accordance with a compliance framework, the accompanying financial statements have not been prepared, in all material respects, in accordance with [the applicable financial reporting framework].

5.8.3 What special consideration is required for expressing Disclaimer of Opinion?

When the auditor disclaims an opinion due to an inability to obtain sufficient appropriate audit evidence, the auditor shall:

(a) State that the auditor does not express an opinion on the accompanying financial statements;

(b) State that, because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and

(c) Amend the statement required in SA 700 (Revised), which indicates that the financial statements have been audited, to state that the auditor was engaged to audit the financial statements.

(d) Unless required by law or regulation, when the auditor disclaims an opinion on the financial statements, the auditor's report shall not include a Key Audit Matters section in accordance with SA 701.

5.8.4 What is the Basis for Modification of Opinion (Qualified/ Disclaimer /Adverse)?

When the auditor modifies (Qualification/ Disclaimer/ Adverse) the opinion as above on the financial statements, the auditor shall, in addition to the specific elements required by SA 700 (Revised):

(a) Amend the heading "Basis for Opinion" to "Basis for Qualified Opinion," "Basis for Adverse Opinion," or "Basis for Disclaimer of Opinion," as appropriate; and

(b) Within this section, include a description of the matter giving rise to the modification.

If there is a material misstatement of the financial statements that relates to specific amounts in the financial statements (including quantitative disclosures in the notes to the financial statements), the auditor shall include in the Basis for Opinion section, a description and quantification of the financial effects of the misstatement, unless impracticable. If it is not practicable to quantify the financial effects, the auditor shall so state in this section.

If there is a material misstatement of the financial statements that relates to narrative disclosures, the auditor shall include in the Basis for Opinion section an explanation of how the disclosures are misstated.

If there is a material misstatement of the financial statements that relates to the non- disclosure of information required to be disclosed, the auditor shall:

(a) Discuss the non-disclosure with those charged with governance;

(b) Describe in the Basis for Opinion section the nature of the omitted information; and

(c) Unless prohibited by law or regulation, include the omitted disclosures, provided it is practicable to do so and the auditor has obtained sufficient appropriate audit evidence about the omitted information.

If the modification results from an inability to obtain sufficient appropriate audit evidence, the auditor shall include in the Basis for Opinion section the reasons for that inability.

When the auditor expresses a qualified or adverse opinion, the auditor shall amend the statement about whether the audit evidence obtained is sufficient & appropriate to provide a basis for the auditor's opinion to include the word "qualified" or "adverse", as appropriate.

When the auditor disclaims an opinion on the financial statements, the auditor's report shall not include following elements required under SA 700

(a) A reference to the section of the auditor's report where the auditor's responsibilities are described; and

(b) A statement about whether the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion.

5.8.5 **Matrix to be considered to determine what type of modified opinion should be used by the Auditor:** When the auditor concludes that there exists a material misstatement which precludes the auditor from issuing an un-modified opinion, the auditor must determine which type of modified opinion is to be issued by the auditor as per SA 705 - Modifications to the Opinion in the Independent Auditors Report. The following matrix assists the auditor in determining the type of modified opinion.

Nature of Matter Giving Rise to the Modification:	Auditor's judgment about the Pervasiveness of the Effects or Possible Effects on the Financial Statements	
	Material but not pervasive	Material and pervasive
Financial Statements are materially misstated	Qualified Opinion	Adverse Opinion
Inability to obtain Sufficient appropriate audit evidence	Qualified Opinion	Disclaimer of Opinion

5.9 Communication with Those Charged with Governance

When the auditor expects to modify the opinion in the auditor's report, the auditor shall communicate with those charged with governance the circumstances that led to the expected modification and the wording of the modification.

6. SA 706, "EMPHASIS OF MATTER PARAGRAPHS AND OTHER MATTER PARAGRAPHS IN THE INDEPENDENT AUDITOR'S REPORT"

6.1 Objective

(a) A matter, although appropriately presented or disclosed in the financial statements, that is of such importance that it is fundamental to users' understanding of the financial statements; or

(b) As appropriate, any other matter that is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

6.2 When to give Emphasis of Matter Paragraphs in the Auditor's Report?

If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to users' understanding of the financial statements, the auditor shall include an Emphasis of Matter paragraph in the auditor's report provided:

(a) The auditor would not be required to modify the opinion in accordance with SA 705 (Revised) as a result of the matter; and

(b) When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the auditor's report.

6.3 When the auditor includes an Emphasis of Matter paragraph in the auditor's report, the auditor shall:

(a) Include the paragraph within a separate section of the auditor's report with an appropriate heading that includes the term "Emphasis of Matter";

(b) Include in the paragraph a clear reference to the matter being emphasized and to where relevant disclosures that fully describe the matter can be found in the financial statements. The paragraph shall refer only to information presented or disclosed in the financial statements; and

(c) Indicate that the auditor's opinion is not modified in respect of the matter emphasized.

6.4 When to issue Other Matter Paragraphs in the Auditor's Report?

If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report, the auditor shall include an Other Matter paragraph in the auditor's report, provided:

(a) This is not prohibited by law or regulation; and

(b) When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the auditor's report.

When the auditor includes an Other Matter paragraph in the auditor's report, the auditor shall include the paragraph within a separate section with the heading "Other Matter," or other appropriate heading.

6.5 Is there any duty to communicate with Those Charged with Governance?

If the auditor expects to include an Emphasis of Matter or an Other Matter paragraph in the auditor's report, the auditor shall communicate with those charged with governance regarding this expectation and the wording of this paragraph.

7. DISTINCTION BETWEEN NOTES ON ACCOUNTS AND QUALIFICATIONS

As a general practice, the management would normally prefer to explain their view point and assessment on all matters involving difference of opinion between them and the auditors by way of notes in the financial statements, for better understanding of the facts of the matters by users of financial statements. Such notes represents management's stand on the matter while the auditor records his disagreement on the matters by way of qualifications in the auditor's report.

8. DISTINCTION BETWEEN AUDIT REPORT AND CERTIFICATE

The term 'report' is used where an expression of opinion is involved. The term 'certificate' is preferable where the auditor comments on or verifies facts such as a verification of investment by inspection or the checking of ballot papers on a poll in a company meeting. Under the Companies Act, 2013, a number of situations are there where an auditor is required to issue a certificate rather than a report, like under Section 66 of the Companies Act, 2013, an auditor is required to file a certificate in the tribunal where company is proposing for the reduction of capital. However, the report under Section 143 of the Companies Act, 2013, is an opinion-based report and is not a certificate.

9. COMMUNICATION TO MANAGEMENT AND THOSE CHARGED WITH GOVERNANCE

Refer Chapter 2 Paragraph 4

10. REPORTING REQUIREMENTS IN CASE OF COMPARATIVE INFORMATION

SA 710 Comparative Information-Corresponding Figures and Comparative Financial Statements deals with auditor's responsibility regarding comparative information in an audit of financial statement. There are two different broad approaches to the auditor's responsibilities in respect of comparative information: Corresponding figures and Comparative financial statement.

The essential audit reporting differences between the approaches are:

(a) For corresponding figures, the auditor's opinion on the financial statements refers to the current period only; whereas

(b) For comparative financial statements, the auditor's opinion refers to each period for which financial statements are presented.

10.1 Audit Procedures for Comparative Information:

(a) **Perform Specific audit Procedure:** For determining that the financial statement contains appropriately classified comparative information, the auditor should:

- Ensure that comparative information agrees with the amount and other disclosure presented in the prior period.
- The accounting policies applied are consistent with those applied in current period.
- If there have been any changes in the application of accounting policies than they are properly disclosed and presented.

(b) **Evaluating the impact on financial statement:** The auditor becomes aware of any possible misstatement in the comparative information, then:

- He should perform the necessary audit procedures to obtain sufficient audit evidence.
- If the auditor had audited the prior period's financial statement than he should follow the relevant requirements of SA 560.

(c) **Written Representation:** As required by SA 580, the auditor should also request written representation. He should also obtain a specific written representation regarding any prior period item that is disclosed in current year's financial statement.

10.2 Audit Reporting

(a) **With Reference to Corresponding Figures:** When corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in the following circumstances:

- If the auditor's report of the previous period contains other than an unqualified opinion.
- If the auditor is of the opinion, and he has sufficient evidence in this regard, that a material misstatement exists in the financial statement of prior period, which was not addressed earlier.

If the prior period financial statement are not audited, than he should obtain sufficient audit evidence that the opening balance does not contain any material misstatement.

(b) With Reference to Comparative Financial Statement: *When comparative financial statement are presented -*

- *The auditor's opinion shall refer to each period for which the financial statements are presented.*
- *When reporting on current period's audit, if the auditor's opinion on such prior period financial statement differs from the opinion previously issued on such financial statement, the auditor shall disclose the substantive reason for the different opinion in other matter paragraph in his report.*
- *If the auditor concludes that a material misstatement is present in the previously audited figures of financial statement, he should report it to the appropriate level of the management and request that the predecessor auditor be informed. If then the prior year's statements are amended with new report by the predecessor auditor, then the auditor shall report only on the current period.*

(c) Reporting treatment common to both (for corresponding figures and comparative information):

(i) *If the financial statement of the prior period were audited by a predecessor auditor, the auditor (is permitted by law or regulation to refer to the predecessor audit report – on case of corresponding figures and decides to do so) shall state in his audit report:*

- *That the financial statement of the prior period were audited by a predecessor auditor;*
- *The type of the opinion expressed by the predecessor auditor;*
- *The date of that audit report.*

(ii) *If the prior period financial statement were not audited than he shall report the same in other matter paragraph in his audit report that the corresponding/comparative figures are unaudited. However, the disclosure does not relieve him from his responsibility of obtaining sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements.*

11. SA 720, "THE AUDITORS' RESPONSIBILITIES RELATING TO OTHER INFORMATION"

This SA does not apply to preliminary announcements of financial information; or securities offering documents, including prospectuses.

Important Definition:

(a) **Annual report-** A document, or combination of documents, prepared typically on an annual basis by management or those charged with governance in accordance with law, regulation or custom, the purpose of which is to provide owners (or similar stakeholders) with information on the entity's operations and the entity's financial results and financial position as set out in the financial statements. An annual report contains or accompanies the financial statements and the auditor's report thereon and usually includes information about the entity's developments, its future outlook and risks and uncertainties, a statement by the entity's governing body, and reports covering governance matters.

(b) **Other information-** Financial or non-financial information (other than financial statements and the auditor's report thereon) included in an entity's annual report.

11.1 Objective

The objectives of the auditor, having read the other information, are:

(a) To consider whether there is a material inconsistency between the other information and the financial statements;

(b) To consider whether there is a material inconsistency between the other information and the auditor's knowledge obtained in the audit;

(c) To respond appropriately when the auditor identifies that such material inconsistencies appear to exist, or when the auditor otherwise becomes aware that other information appears to be materially misstated; and

(d) To report in accordance with this SA.

11.2 Obtaining the Other Information

The auditor shall:

(a) Determine, through discussion with management, which document(s) comprises the annual report, and the entity's planned manner and timing of the issuance of such document(s);

(b) Make appropriate arrangements with management to obtain in a timely manner and, if possible, prior to the date of the auditor's report, the final version of the document(s) comprising the annual report; and

(c) When some or all of the document(s) determined in (a) will not be available until after the date of the auditor's report, request management to provide a written representation that the final version of the document(s) will be provided to the auditor when available, and prior to its issuance by the entity, such that the auditor can complete the procedures required by this SA.

Reading and Considering the Other Information

The auditor shall read the other information and, in doing so shall:

(a) Consider whether there is a material inconsistency between the other information and the financial statements. As the basis for this consideration, the auditor shall, to evaluate their consistency, compare selected amounts or other items in the other information (that are intended to be the same as, to summarize, or to provide greater detail about, the amounts or other items in the financial statements) with such amounts or other items in the financial statements; and

(b) Consider whether there is a material inconsistency between the other information and the auditor's knowledge obtained in the audit, in the context of audit evidence obtained and conclusions reached in the audit.

11.3 Responding When a Material Inconsistency Appears to Exist or Other Information Appears to Be Materially Misstated

If the auditor identifies that a material inconsistency appears to exist (or becomes aware that the other information appears to be materially misstated), the auditor shall discuss the matter with management and, if necessary, perform other procedures to conclude whether:

(a) A material misstatement of the other information exists;

(b) A material misstatement of the financial statements exists; or

(c) The auditor's understanding of the entity and its environment needs to be updated.

11.4 Responding When the Auditor Concludes That a Material Misstatement of the Other Information Exists

11.4.1 If the auditor concludes that a material misstatement of the other information exists, the auditor shall request management to correct the other information. If management:

(a) Agrees to make the correction, the auditor shall determine that the correction has been made; or

(b) Refuses to make the correction, the auditor shall communicate the matter with those charged with governance and request that the correction be made.

11.4.2 If the auditor concludes that a material misstatement exists in other information obtained prior to the date of the auditor's report, and the other information is not corrected after communicating with those charged with governance, the auditor shall take appropriate action, including:

(a) Considering the implications for the auditor's report and communicating with those charged with governance about how the auditor plans to address the material misstatement in the auditor's report.

(b) Withdrawing from the engagement, where withdrawal is possible under applicable law or regulation.

11.4.3 If the auditor concludes that a material misstatement exists in other information obtained after the date of the auditor's report, the auditor shall:

(a) If the other information is corrected, perform the procedures necessary in the circumstances; or

(b) If the other information is not corrected after communicating with those charged with governance, take appropriate action considering the auditor's legal rights and obligations, to seek to have the uncorrected material misstatement appropriately brought to the attention of users for whom the auditor's report is prepared.

11.5 Responding When a Material Misstatement in the Financial Statements Exists or the Auditor's Understanding of the Entity and Its Environment Needs to Be Updated

If, as a result of performing the procedures discussed in 11.2, the auditor concludes that a material misstatement in the financial statements exists or the auditor's understanding of the entity and its environment needs to be updated, the auditor shall respond appropriately in accordance with the other SAs.

11.6 Reporting

The auditor's report shall include a separate section with a heading "Other Information", or other appropriate heading, when, at the date of the auditor's report:

(a) For an audit of financial statements of a listed entity, the auditor has obtained, or expects to obtain, the other information; or

(b) For an audit of financial statements of an unlisted corporate entity, the auditor has obtained some or all of the other information.

When the auditor's report is required to include an Other Information section, this section shall include:

(a) A statement that management is responsible for the other information;

(b) An identification of:

(i) Other information, if any, obtained by the auditor prior to the date of the auditor's report; and

(ii) For an audit of financial statements of a listed entity, other information, if any, expected to be obtained after the date of the auditor's report;

(c) A statement that the auditor's opinion does not cover the other information and, accordingly, that the auditor does not express (or will not express) an audit opinion or any form of assurance conclusion thereon;

(d) A description of the auditor's responsibilities relating to reading, considering and reporting on other information as required by this SA; and

(e) When other information has been obtained prior to the date of the auditor's report, either:

(i) A statement that the auditor has nothing to report; or

(ii) If the auditor has concluded that there is an uncorrected material misstatement of the other information, a statement that describes the uncorrected material misstatement of the other information.

11.7 Reporting Prescribed by Law or Regulation

If the auditor is required by a relevant law or regulation to refer to the other information in the auditor's report using a specific layout or wording, the auditor's report shall refer to Standards on Auditing only if the auditor's report includes, at a minimum:

(a) Identification of the other information obtained by the auditor prior to the date of the auditor's report;

(b) A description of the auditor's responsibilities with respect to the other information; and

(c) An explicit statement addressing the outcome of the auditor's work for this purpose.

12. DUTIES OF AUDITORS

Sections 143 of the Companies Act, 2013 specifies the duties of an auditor of a company in a quite comprehensive manner. It is noteworthy that scope of duties of an auditor has generally been extending over all these years.

1. **Duty of Auditor to Inquire on certain matters:** It is the duty of auditor to inquire into the following matters-

(a) whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members;

(b) whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company;

(c) where the company not being an investment company or a banking company, whether so much of the assets of the company as consist of shares, debentures and other securities have been sold at a price less than that at which they were purchased by the company;

(d) whether loans and advances made by the company have been shown as deposits;

(e) whether personal expenses have been charged to revenue account;

(f) where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading.

2. **Duty to Sign the Audit Report:** As per section 145 of the Companies Act, 2013, the person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document of the company, in accordance with the provisions of sub-section (2) of section 141 and the qualifications, observations or comments on

financial transactions or matters, which have any adverse effect on the functioning of the company mentioned in the auditors' report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

3. **Duty to comply with Auditing Standards:** As per sub-section (9) of section 143 of the Companies Act, 2013, every auditor shall comply with the auditing standards.

4. **Duty to audit report:** As per sub-section (3) of section 143, the auditor's report shall also state-

(a) whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;

(b) whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books & proper returns adequate for the purposes of his audit have been received from branches not visited by him;

(c) whether the report on the accounts of any branch office of the company audited under sub- section (8) by a person other than the company's auditors has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;

(d) whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;

(e) whether, in his opinion, the financial statements comply with the accounting standards;

(f) the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;

(g) whether any director is disqualified from being appointed as a director under sub-section (2) of the section 164;

(h) any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;

(i) whether the company has adequate internal financial controls with reference to financial statements in place and the operating effectiveness of such controls;

(Note: Clause (i) of Sub-Section (3) of Section143 shall not apply to a private company: - (i) which is a one person company or a small company; or (ii) which has turnover less than rupees fifty crores as per latest audited financial statement and which has aggregate borrowings from banks or financial institutions or anybody corporate at any point of time during the financial year less than rupees twenty five crore)

(j) such other matters as may be prescribed. Rule 11 of the Companies (Audit and Auditors) Rules, 2014 prescribes the other matters to be included in auditor's report. The auditor's report shall also include their views and comments on the following matters, namely:-

(1) whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;

(2) whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;

(3) whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.

(4)

(i) Whether the management has represented that, to the best of it's knowledge and belief, other than as disclosed in the notes to the accounts, no funds have been advanced or loaned or invested (either from borrowed funds or share premium or any other sources or kind of funds) by the company to or in any other person(s) or entity(ies), including foreign entities ("Intermediaries"), with the understanding, whether recorded in writing or otherwise, that the Intermediary shall, whether, directly or indirectly lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the company ("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries;

(ii) Whether the management has represented, that, to the best of it's knowledge and belief, other than as disclosed in the notes to the accounts, no funds have been received by the company from any person(s) or entity(ies), including foreign entities ("Funding Parties"), with the understanding, whether recorded in writing or otherwise, that the company shall, whether, directly or indirectly, lend or invest in other persons *or entities identified in any manner whatsoever by or on behalf of the Funding Party ("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries; and*

(iii) Based on such audit procedures that the auditor has considered reasonable and appropriate in the circumstances, nothing has come to their notice that has caused them to believe that the representations under sub-clause (i) and (ii) contain any material mis-statement.

(5) Whether the dividend declared or paid during the year by the company is in compliance with section 123 of the Companies Act, 2013.

(6) Whether the company has used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and the same has been operated throughout the year for all transactions recorded in the software and the audit trail feature has not been tampered with and the audit trail has been preserved by the company as per the statutory requirements for record retention.]

Audit Trail means, a step by step sequential record which provides evidence of the documented history of financial transactions to its source. An auditor can trace every step of, the financial data of a particular transaction right from the general ledger to its source document with the help of the audit trail.

The Companies (Amendment) Act, 2017 effective 12-09-2018 inserted Section 197(16) of the Companies Act, 2013 that requires as under:

"The auditor of the company shall, in his report under section 143, make a statement as to whether the remuneration paid by the company to its directors is in accordance with the provisions of this section, whether remuneration paid to any director is in excess of the limit laid down under this section and give such other details as may be prescribed".

5. Duty to report on frauds:

A. Reporting to the Central Government: *As per sub-section (12) of section 143 of the Companies Act, 2013, if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud involving such* amount or amounts as may be prescribed, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time and in such manner as may be prescribed.

In this regard, Rule 13 of the Companies (Audit and Auditors) Rules, 2014 has been prescribed. Sub-rule (1) of the Rule 13 states that if an auditor of a company, in the course of the performance of his duties as statutory auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of ₹ 1 crore or above, is being or has been committed against the company by its officers or employees, the auditor shall report the matter to the Central Government.

The manner of reporting the matter to the Central Government is as follows:

(a) the auditor shall report the matter to the Board or the Audit Committee, as the case may be, immediately but not later than 2 days of his knowledge of the fraud, seeking their reply or observations within 45 days;

(b) on receipt of such reply or observations, the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the Central Government within 15 days from the date of receipt of such reply or observations;

(c) in case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of 45 days, he shall forward his report to the Central Government along with a note containing the details of his report that was earlier forwarded to the Board or the Audit Committee for which he has not received any reply or observations;

(d) the report shall be sent to the Secretary, Ministry of Corporate Affairs in a sealed cover by Registered Post with Acknowledgement Due or by Speed Post followed by an e-mail in confirmation of the same;

(e) the report shall be on the letter-head of the auditor containing postal address, e-mail address and contact telephone number or mobile number and be signed by the auditor with his seal and shall indicate his Membership Number; and

(f) the report shall be in the form of a statement as specified in Form ADT-4.

B. Reporting to the Audit Committee or Board- Sub-section (12) of section 143 of the Companies Act, 2013 further prescribes that in case of a fraud involving lesser than the specified amount [i.e. less than ₹ 1 crore], the auditor shall report the matter to the audit committee constituted under section 177 or to the Board in other cases within such time and in such manner as may be prescribed.

In this regard, sub-rule (3) of Rule 13 of the Companies (Audit and Auditors) Rules, 2014 states that in case of a fraud involving lesser than the amount specified in sub-rule (1) [i.e. less than ₹ 1 crore], the auditor shall report the matter to Audit Committee constituted under section 177 or to the Board immediately but not later than 2 days of his knowledge of the fraud and he shall report the matter specifying the following:

(a) Nature of Fraud with description;	(b) Approximate amount involved; and	(c) Parties involved.

C. Disclosure in the Board's Report: Sub-section (12) of section 143 of the Companies Act, 2013 furthermore prescribes that the companies, whose auditors have reported frauds under this sub- section (12) to the audit committee or the Board, but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in such manner as may be prescribed.

In this regard, sub-rule (4) of Rule 13 of the Companies (Audit and Auditors) Rules, 2014 states that the company is required to disclose in the Board's Report the following details of each of the fraud reported to the Audit Committee or the Board under sub-rule (3) during the year:

(a) Nature of Fraud with description;	(b) Approximate Amount involved;
(c) Parties involved, if remedial action not taken; and	(d) Remedial actions taken.

Sub-section (13) of section 143 of the Companies Act, 2013 safeguards the act of fraud reporting by the auditor if it is done in good faith. It states that no duty to which an auditor of a company may be subject to shall be regarded as having been contravened by reason of his reporting the matter above if it is done in good faith.

It is very important to note that the provisions regarding fraud reporting shall also apply, mutatis mutandis, to a cost auditor and a secretarial auditor during the performance of his duties under section 148 and section 204 respectively. If any auditor, cost accountant or company secretary in practice does not comply with the provisions of sub-section (12) of section 143, he shall be liable to a penalty of five lakh rupees in case of a listed company and a penalty of one lakh rupees in case of any other company.

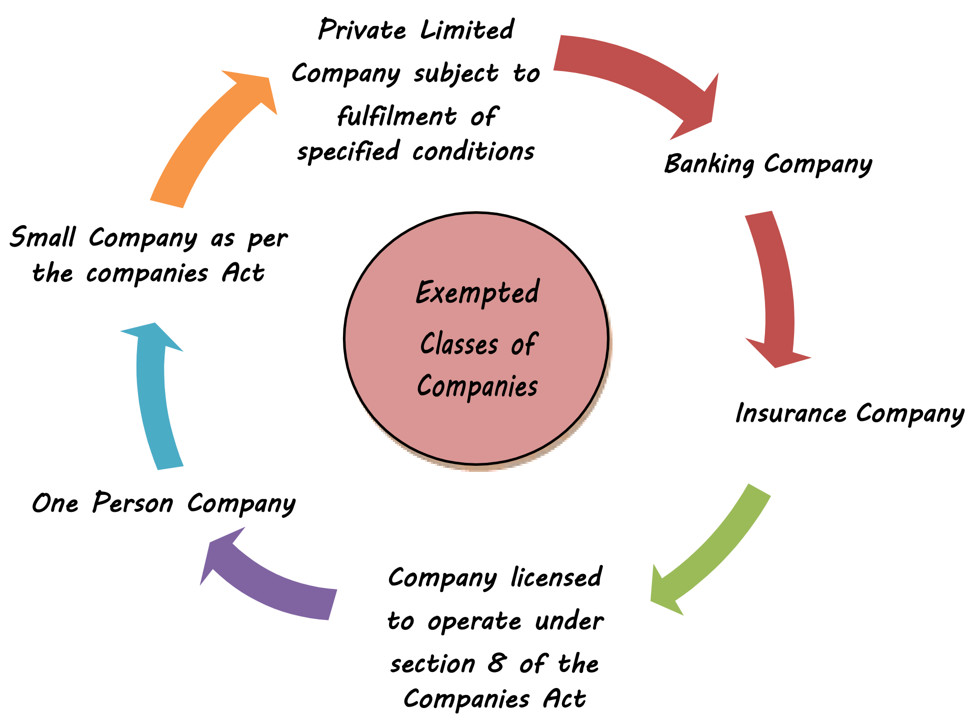
6. **Duty to report on any other matter specified by Central Government:** Central Government may, in consultation with the National Financial Reporting Authority (NFRA), by general or special order, direct, in respect of such class or description of companies, as may be specified in the order, that the auditor's report shall also include a statement on such matters as may be specified therein.

7. **Duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor are discussed separately.**

8. **Duty to state the reason for qualification or negative report:** As per sub-section (4) of section 143, where any of the matters required to be included in the audit report is answered in the negative or with a qualification, the report shall state the reasons there for.

12.1 Reporting Under CARO, 2200

1. **Applicability of the Order:** The CARO, 2020 is an additional reporting requirement. The order applies to every company including a foreign company as defined in clause (42) of section 2 of the Companies Act, 2013. However, the Order specifically **exempts the following classes of companies.**



(i) a banking company as defined in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949);

(ii) an insurance company as defined under the Insurance Act,1938 (4 of 1938);

(iii) a company licensed to operate under section 8 of the Companies Act;

(iv) a One Person Company as defined under clause (62) of section 2 of the Companies Act and a small company as defined under clause (85) of section 2 of the Companies Act; and

(v) a private limited company, not being a subsidiary or holding company of a public company, having a paid up capital and reserves and surplus not more than rupees one crore as on the balance sheet date and which does not have total borrowings exceeding rupees one crore from any bank or financial institution at any point of time during the financial year and which does not have a total revenue as disclosed in Scheduled III to the Companies Act, 2013 (including revenue from discontinuing operations) exceeding rupees ten crore during the financial year as per the financial statements.

2. **Auditor's report to contain matters specified in paragraphs 3 and 4:** Every report made by the auditor under section 143 of the Companies Act, 2013 on the accounts

of every company audited by him, to which this Order applies, for the financial year, shall in addition, contain the matters specified in paragraphs 3 and 4, as may be applicable.

It may be noted that the Order shall not apply to the auditor's report on consolidated financial statements except clause (xxi) of paragraph 3.

3. **Matters to be included in the auditor's report:** The auditor's report on the accounts of a company to which this Order applies shall include a statement on the following matters, namely:-

(i) (a) (A) whether the company is maintaining proper records showing full particulars, including quantitative details and situation of Property, Plant and Equipment;

(B) Whether the company is maintaining proper records showing full particulars of intangible assets;

(b) Whether these Property, Plant and Equipment have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account;

(c) whether the title deeds of all the immovable properties (other than properties where the company is the lessee and the lease agreements are duly executed in favour of the lessee) disclosed in the financial statements are held in the name of the company, if not, provide the details thereof in the format below:-

Description of property	Gross carrying value	Held in name of	Whether promoter, director or their relative or employee	Period held – indicate range, where appropriate	Reason for not being held in name of company*
-	-	-	-	-	*also indicate if in dispute

(d) whether the company has revalued its Property, Plant and Equipment (including Right of Use assets) or intangible assets or both during the year and, if so, whether the revaluation is based on the valuation by a Registered Valuer; specify the amount of change, if change is 10% or more in the aggregate of the net carrying value of each class of Property, Plant and Equipment or intangible assets;

(e) Whether any proceedings have been initiated or are pending against the company for holding any benami property under the Benami Transactions (Prohibition) Act, 1988 (45 of 1988) and rules made thereunder, if so, whether the company has appropriately disclosed the details in its financial statements;

(ii) (a) Whether physical verification of inventory has been conducted at reasonable intervals by the management and whether, in the opinion of the auditor, the coverage and procedure of such verification by the management is appropriate; whether any discrepancies of 10% or more in the aggregate for each class of inventory were noticed and if so, whether they have been properly dealt with in the books of account;

(b) Whether during any point of time of the year, the company has been sanctioned working capital limits in excess of five crore rupees, in aggregate, from banks or financial institutions on the basis of security of current assets; whether the quarterly returns or statements filed by the company with such banks or financial institutions are in agreement with the books of account of the Company, if not, give details;

(iii) Whether during the year the company has made investments in, provided any guarantee or security or granted any loans or advances in the nature of loans, secured or unsecured, to companies, firms, Limited Liability Partnerships or any other parties, if so,-

(a) whether during the year the company has provided loans or provided advances in the nature of loans, or stood guarantee, or provided security to any other entity [not applicable to companies whose principal business is to give loans], if so, indicate-

- the aggregate amount during the year, and balance outstanding at the balance sheet date with respect to such loans or advances and guarantees or security to subsidiaries, joint ventures and associates;
- the aggregate amount during the year, and balance outstanding at the balance sheet date with respect to such loans or advances and guarantees or security to parties other than subsidiaries, joint ventures and associates;

(b) whether the investments made, guarantees provided, security given and the terms and conditions of the grant of all loans and advances in the nature of loans and guarantees provided are not prejudicial to the company's interest;

(c) in respect of loans and advances in the nature of loans, whether the schedule of repayment of principal and payment of interest has been stipulated and whether the repayments or receipts are regular;

(d) if the amount is overdue, state the total amount overdue for more than ninety days, and whether reasonable steps have been taken by the company for recovery of the principal and interest;

(e) whether any loan or advance in the nature of loan granted which has fallen due during the year, has been renewed or extended or fresh loans granted to settle the over dues of existing loans given to the same parties, if so, specify the aggregate amount of such dues renewed or extended or settled by fresh loans and the percentage of the aggregate to the total loans or advances in the nature of loans granted during the year [not applicable to companies whose principal business is to give loans];

(f) whether the company has granted any loans or advances in the nature of loans either repayable on demand or without specifying any terms or period of repayment, if so, specify the aggregate amount, percentage thereof to the total loans granted, aggregate amount of loans granted to Promoters, related parties as defined in clause (76) of section 2 of the Companies Act, 2013;

(iv) in respect of loans, investments, guarantees, and security, whether provisions of sections 185 and 186 of the Companies Act have been complied with, if not, provide the details thereof;

(v) in respect of deposits accepted by the company or amounts which are deemed to be deposits, whether the directives issued by the Reserve Bank of India and the provisions of sections 73 to 76 or any other relevant provisions of the Companies Act and the rules made thereunder, where applicable, have been complied with, if not, the nature of such contraventions be stated; if an order has been passed by Company Law Board or National Company Law Tribunal or Reserve Bank of India or any court or any other tribunal, whether the same has been complied with or not;

(vi) whether maintenance of cost records has been specified by the Central Government under sub-section (1) of section 148 of the Companies Act and whether such accounts and records have been so made and maintained

(vii) (a) whether the company is regular in depositing undisputed statutory dues including Goods and Services Tax, provident fund, employees' state insurance, income-tax, sales-tax, service tax, duty of customs, duty of excise, value added tax, cess and any other statutory dues to the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as on the last day of the financial year concerned for a period of more than six months from the date they became payable, shall be indicated;

(b) where statutory dues referred to in sub-clause (a) have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned (a mere representation to the concerned Department shall not be treated as a dispute);

(viii) whether any transactions not recorded in the books of account have been surrendered or disclosed as income during the year in the tax assessments under the Income Tax Act, 1961 (43 of 1961), if so, whether the previously unrecorded income has been properly recorded in the books of account during the year;

(ix) (a) whether the company has defaulted in repayment of loans or other borrowings or in the payment of interest thereon to any lender, if yes, the period and the amount of default to be reported as per the format below:-

Nature of borrowing, including debt securities	Name of lender*	Amount not paid on due date	Whether principal or interest	No. of days delay or unpaid	Remarks, if any
	*lender wise details to be provided in case of defaults to banks, financial institutions and Government.				

(b) whether the company is a declared wilful defaulter by any bank or financial institution or other lender;

(c) whether term loans were applied for the purpose for which the loans were obtained; if not, the amount of loan so diverted and the purpose for which it is used may be reported;

(d) whether funds raised on short term basis have been utilised for long term purposes, if yes, the nature and amount to be indicated;

(e) whether the company has taken any funds from any entity or person on account of or to meet the obligations of its subsidiaries, associates or joint ventures, if so, details thereof with nature of such transactions and the amount in each case;

(f) whether the company has raised loans during the year on the pledge of securities held in its subsidiaries, joint ventures or associate companies, if so, give details thereof and also report if the company has defaulted in repayment of such loans raised;

(x) (a) whether moneys raised by way of initial public offer or further public offer (including debt instruments) during the year were applied for the purposes for which those are raised, if not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported;

(b) whether the company has made any preferential allotment or private placement of shares or convertible debentures (fully, partially or optionally convertible) during the year and if so, whether the requirements of section 42 and section 62 of the Companies Act, 2013 have been complied with and the funds raised have been used for the purposes for which the funds were raised, if not, provide details in respect of amount involved and nature of non-compliance;

(xi) (a) Whether any fraud by the company or any fraud on the company has been noticed or reported during the year, if yes, the nature and the amount involved is to be indicated;

(b) Whether any report under sub-section (12) of section 143 of the Companies Act has been filed by the auditors in Form ADT-4 as prescribed under rule 13 of Companies (Audit and Auditors) Rules, 2014 with the Central Government;

(c) Whether the auditor has considered whistle-blower complaints, if any, received during the year by the company;

(xii) (a) Whether the Nidhi Company has complied with the Net Owned Funds to Deposits in the ratio of 1:20 to meet out the liability;

(b) Whether the Nidhi Company is maintaining ten per cent. unencumbered term deposits as specified in the Nidhi Rules, 2014 to meet out the liability;

(c) Whether there has been any default in payment of interest on deposits or repayment thereof for any period and if so, the details thereof;

(xiii) Whether all transactions with the related parties are in compliance with sections 177 and 188 of Companies Act where applicable and the details have been disclosed in the financial statements, etc., as required by the applicable accounting standards;

(xiv) (a) Whether the company has an internal audit system commensurate with the size and nature of its business;

(b) Whether the reports of the Internal Auditors for the period under audit were considered by the statutory auditor;

(xv) Whether the company has entered into any non-cash transactions with directors or persons connected with him and if so, whether the provisions of section 192 of Companies Act have been complied with;

(xvi) (a) Whether the company is required to be registered under section 45-IA of the Reserve Bank of India Act, 1934 (2 of 1934) and if so, whether the registration has been obtained;

(b) Whether the company has conducted any Non-Banking Financial or Housing Finance activities without a valid Certificate of Registration (COR) from the Reserve Bank of India as per the Reserve Bank of India Act, 1934;

(c) Whether the company is a Core Investment Company (CIC) as defined in the regulations made by the Reserve Bank of India, if so, whether it continues to fulfil the criteria of a CIC, and in case the company is an exempted or unregistered CIC, whether it continues to fulfil such criteria;

(d) Whether the Group has more than one CIC as part of the Group, if yes, indicate the number of CICs which are part of the Group;

(xvii) Whether the company has incurred cash losses in the financial year and in the immediately preceding financial year, if so, state the amount of cash losses;

(xviii) Whether there has been any resignation of the statutory auditors during the year, if so, whether the auditor has taken into consideration the issues, objections or concerns raised by the outgoing auditors;

(xix) On the basis of the financial ratios, ageing and expected dates of realisation of financial assets and payment of financial liabilities, other information accompanying the financial statements, the auditor's knowledge of the Board of Directors and management plans, whether the auditor is of the opinion that no material uncertainty exists as on the date of the audit report that company is capable of meeting its liabilities existing at the date of balance sheet as and when they fall due within a period of one year from the balance sheet date;

(xx) (a) Whether, in respect of other than ongoing projects, the company has transferred unspent amount to a Fund specified in Schedule VII to the Companies Act within a period of six months of the expiry of the financial year in compliance with second proviso to sub-section (5) of section 135 of the said Act;

(b) Whether any amount remaining unspent under sub-section (5) of section 135 of the Companies Act, pursuant to any ongoing project, has been transferred to special account in compliance with the provision of sub-section (6) of section 135 of the said Act;

(xxi) Whether there have been any qualifications or adverse remarks by the respective auditors in the Companies (Auditor's Report) Order (CARO) reports of the companies included in the consolidated financial statements, if yes, indicate the details of the companies and the paragraph numbers of the CARO report containing the qualifications or adverse remarks.

4. Reasons to be stated for unfavourable or qualified answers:

(a) Where, in the auditor's report, the answer to any of the questions referred to in paragraph 3 is unfavourable or qualified, the auditor's report shall also state the basis for such unfavourable or qualified answer, as the case may be.

(b) Where the auditor is unable to express any opinion on any specified matter, his report shall indicate such fact together with the reasons as to why it is not possible for him to give his opinion on the same.

8. SPECIALISED AREAS

1. INTRODUCTION

- SA 800 deals with special considerations applicable in respect of the audit of financial statements prepared in accordance with the special purpose framework.
- SA 805 deals with special considerations applicable to an audit of a single financial statement or of a specific element, account or item of a financial statement.
- SA 810 deals with responsibilities of an auditor when undertaking an engagement to report on summary financial statements derived from financial statements audited in accordance with SAs by that same auditor.

2. SA 800 - SPECIAL CONSIDERATIONS AUDITS OF FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH SPECIAL PURPOSE FRAMEWORKS

SA 800 addresses special considerations that are relevant to: -

(a) The acceptance of the engagement

(b) The planning and performance of that engagement and

(c) Forming an opinion and reporting on the financial statements but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

2.1 What is Special Purpose framework?

Special purpose framework is to be distinguished from general purpose framework. A financial reporting framework designed to meet the common financial information needs of a wide range of users is known as "General purpose framework" whereas a financial reporting framework designed to meet the financial information needs of specific users is known as "Special purpose framework."

2.2 Considerations When Accepting Such Engagement

In the case of special purpose financial statements, the financial information needs of the intended users are a key factor in determining the acceptability of the financial reporting framework applied in the preparation of the financial statements.

In that case, those standards will be presumed acceptable for that purpose if the organisation follows an established and transparent process involving deliberation and consideration of the views of relevant stakeholders.

In the case of a special purpose framework, the relative importance to a particular engagement of each of the attributes normally exhibited by acceptable financial reporting frameworks is a matter of professional judgment.

2.3 Considerations When Planning and Performing Such Audit

(a) SA 200 requires the auditor to comply with (a) relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements, and (b) all SAs relevant to the audit. It also requires the auditor to comply with each requirement of an SA unless, in the circumstances of the audit, the entire SA is not relevant or the requirement is not relevant because it is conditional and the condition does not exist. In exceptional circumstances, the auditor may judge it necessary to depart from a relevant requirement in an SA by performing alternative audit procedures to achieve the aim of that requirement.

Application of some of the requirements of the SAs in an audit of special purpose financial statements may require special consideration by the auditor.

(b) In the case of special purpose financial statements, such as those prepared in accordance with the requirements of a contract, management may agree with the intended users on a threshold below which misstatements identified during the audit will not be corrected or otherwise adjusted. The existence of such a threshold does not relieve the auditor from the requirement to determine materiality in accordance with SA 320 for purposes of planning and performing the audit of the special purpose financial statements.

(c) SA 260 (Revised) requires the auditor to determine the appropriate person(s) within the entity's governance structure with whom to communicate. SA 260 (Revised) notes that, in some cases, all of those charged governance are involved in managing the entity, and the application of the communication requirements is modified to recognize this position. When a complete set of general purpose financial statements is also prepared by the entity, those person(s) responsible for the oversight of the preparation of the special purpose financial statements may not be the same as those charged with governance responsible for the oversight of the preparation of those general purpose financial statements.

(d) **Forming an opinion and reporting considerations in such an audit:** When forming an opinion and reporting on special purpose financial statements, the auditor shall apply the requirements in Revised SA 700.

2.4 Description of the Applicable Financial Reporting Framework

Revised SA 700 deals with the form and content of the auditor's report. In the case of an auditor's report on special purpose financial statements: -

(a) The auditor's report shall also describe the purpose for which the financial statements are prepared and, if necessary, the intended users, or refer to a note in the special purpose financial statements that contain that information; and

(b) If management has a choice of financial reporting frameworks in the preparation of such financial statements, the explanation of management's responsibility for the financial statements shall also make reference to its responsibility for determining that the applicable financial reporting framework is acceptable in the circumstances.

2.5 Alerting Readers that the Financial Statements Are Prepared in Accordance with a Special Purpose Framework

The special purpose financial statements may be used for purposes other than those for which they were intended.

2.6 Restriction on Distribution or Use

In addition to the alert required as discussed above, the auditor may consider it appropriate to indicate that the auditor's report is intended solely for the specific users.

3. SA 805-SPECIAL CONSIDERATIONS AUDITS OF SINGLE FINANCIAL STATEMENTS AND SPECIFIC ELEMENTS, ACCOUNTS OR ITEMS OF A FINANCIAL STATEMENT

SA 805 does not apply to the report of a component auditor issued as a result of work performed on the financial information of a component at the request of a group engagement team for purposes of an audit of group financial statements.

3.1 What is a Single Financial Statement?

A single financial statement is to be distinguished from a complete set of financial statements. **For example,** a cash flow statement is a single financial statement.

3.2 What is the Element of a Financial Statement?

"Element of a financial statement" or "element" means an "element, account or item of a financial statement." For example, trade receivables or cash and bank balances.

A single financial statement or a specific element of a financial statement includes the related notes ordinarily comprising a summary of significant accounting policies and other explanatory information relevant to the financial statement or to the element.

3.3 Considerations When Accepting Such Engagement

3.3.1 Application of SAs

SA 200 requires the auditor to comply with (a) relevant ethical requirements, including those pertaining to independence relating to financial statement audit engagements, and (b) all SAs relevant to the audit.

Compliance with the requirements of SAs relevant to the audit of a single financial statement or of a specific element of a financial statement may not be practicable when the auditor is not also engaged to audit the entity's complete set of financial statements. In such cases, the auditor often does not have the same understanding of the entity and its environment, including its internal control, as an auditor who also audits the entity's complete set of financial statements. Accordingly, the auditor may need further evidence to corroborate audit evidence acquired from the accounting records.

In the case of an audit of a specific element of a financial statement, certain SAs require audit work that may be disproportionate to the element being audited. If the auditor concludes that an audit of a single financial statement or of a specific element of a financial statement in accordance with SAs may not be practicable, the auditor may discuss with management whether another type of engagement might be more practicable.

3.3.2 Acceptability of the Financial Reporting Framework

SA 210 requires the auditor to determine the acceptability of the financial reporting framework applied in the preparation of the financial statements. In the case of an audit of a single financial statement or of a specific element of a financial statement, this shall include 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 in the financial statement or the element, and the effect of material transactions and events on the information conveyed in the financial statement or the element.

A single financial statement or a specific element of a financial statement may be prepared in accordance with an applicable financial reporting framework that is based on a financial reporting framework established by an authorised or recognised standards setting organisation for the preparation of a complete set of financial statements. If this is the case, determination of the acceptability of the applicable framework may involve considering whether that framework includes all the requirements of the framework on which it is based that are relevant to the presentation of a single financial statement or of a specific element of a financial statement that provides adequate disclosures.

3.4 Considerations When planning and performing the Audit

In planning and performing the audit of a single financial statement or of a specific element of a financial statement, the auditor shall adapt all SAs relevant to the audit as necessary in the circumstances of the engagement.

When auditing a single financial statement or a specific element of a financial statement in conjunction with the audit of the entity's complete set of financial statements, the auditor may be able to use audit evidence obtained as part of the audit of the entity's complete set of financial statements in the audit of the financial statement or the element. SAs, however, require the auditor to plan and perform the audit of the financial statement or element to obtain sufficient appropriate audit evidence on which to base the opinion on the financial statement or on the element.

The individual financial statements that comprise a complete set of financial statements, and many of the elements of those financial statements, including their related notes, are interrelated. Accordingly, when auditing a single financial statement or a specific element of a financial statement, the auditor may not be able to consider the financial statement or the element in isolation. Consequently, the auditor may need to perform procedures in relation to the interrelated items to meet the objective of the audit.

Furthermore, the materiality determined for a single financial statement or for a specific element of a financial statement may be lower than the materiality determined for the entity's complete set of financial statements; this will affect the nature, timing and extent of the audit procedures and the evaluation of uncorrected misstatements.

3.5 Form of Opinion

The form of opinion to be expressed by the auditor depends on the applicable financial reporting framework and any applicable laws or regulations.

Factors that may affect the auditor's consideration as to whether to use the phrases "presents fairly, in all material respects", or "gives a true and fair view" in the audit opinion include:

Whether the applicable financial reporting framework is explicitly or implicitly restricted to the preparation of a complete set of financial statements.

Whether the single financial statement or the specific element of a financial statement will:

- Comply fully with each of those requirements of the framework relevant to the particular financial statement or the particular element, and the presentation of the financial statement or the specific element of a financial statement include the related notes and disclosures
- If necessary to achieve fair presentation, provide disclosures beyond those specifically required by the framework or, in exceptional circumstances, depart from a requirement of the framework.

3.6 Forming an Opinion and Reporting Considerations

When forming an opinion and reporting on a single financial statement or on a specific element of a financial statement, the auditor shall apply the requirements in Revised SA 700, adapted as necessary in the circumstances of the engagement.

If the auditor undertakes an engagement to report on a single financial statement or on a specific element of a financial statement in conjunction with an engagement to audit the entity's complete set of financial statements, the auditor shall express a separate opinion for each engagement.

An audited single financial statement or an audited specific element of a financial statement may be published together with the entity's audited complete set of financial statements. If the auditor concludes that the presentation of a single financial statement or of the specific element of a financial statement does not differentiate it sufficiently from the complete set of financial statements, the auditor shall ask management to rectify the situation. The auditor shall also differentiate the opinion on the single financial statement or on the specific element of a financial statement from the opinion on the complete set of financial statements. The auditor shall not issue the auditor's report containing the opinion on the single financial statement or on the specific element of a financial statement until satisfied with the differentiation.

(1) If the opinion in the auditor's report on an entity's complete set of financial statements is modified, or that report includes an Emphasis of matter paragraph or

other matter paragraph, the auditor shall determine the effect that this may have on the auditor's report on a single financial statement or on a specific element of those financial statements. When deemed appropriate, the auditor shall modify the opinion on the single financial statement or on the specific element of a financial statement, or include an Emphasis of matter paragraph or other matter paragraph in the auditor's report, accordingly.

(2) If the auditor concludes that it is necessary to express an adverse opinion or disclaim an opinion on the entity's complete set of financial statements as a whole, Revised SA 705 does not permit the auditor to include in the same auditor's report an unmodified opinion on a single financial statement that forms part of those financial statements or on a specific element that forms part of those financial statements. This is because such an unmodified opinion would contradict the adverse opinion or disclaimer of opinion on the entity's complete set of financial statements as a whole.

(3) If the auditor concludes that it is necessary to express an adverse opinion or disclaim an opinion on the entity's complete set of financial statements as a whole but, in the context of a separate audit of a specific element that is included in those financial statements, the auditor nevertheless considers it appropriate to express an unmodified opinion on that element, the auditor shall only do so if:

(a) The auditor is not prohibited by law or regulation from doing so;

(b) That opinion is expressed in an auditor's report that is not published together with the auditor's report containing the adverse opinion or disclaimer of opinion; and

(c) The specific element does not constitute a major portion of the entity's complete set of financial statements.

In the case of a single financial statement or of a specific element of a financial statement, it is important that the financial statement or the element, including the related notes, in view of the requirements of the applicable financial reporting framework, provides adequate disclosures to enable the intended users to understand the information conveyed in the financial statement or the element, and the effect of material transactions and events on the information conveyed in the financial statement or the element.

In the auditor's report on an entity's complete set of financial statements, the expression of a disclaimer of opinion regarding the results of operations and cash flows, where relevant, and an unmodified opinion regarding the state of affairs is permitted since the disclaimer of opinion is being issued in respect of the results of operations and cash flows only and not in respect of the financial statements as a whole.

SA 800 and 805 do not override the requirements of the other SAs; nor do they purport to deal with all special considerations that may be relevant in the circumstances of the engagement.

4. SA 810 - ENGAGEMENTS TO REPORT ON SUMMARY FINANCIAL STATEMENTS

4.1 What do Summary Financial Statements Reflect?

Summary financial statements reflect historical financial information that is derived from financial statements, but that contains less detail than the financial statements while still providing a structured representation consistent with that provided by the financial statements of the entity's economic resources or obligations at a point in time or the changes therein for a period of time.

4.2 Engagement Acceptance

The auditor shall, ordinarily, accept an engagement to report on summary financial statements in accordance with this SA only when the auditor has been engaged to conduct an audit in accordance with SAs of the financial statements from which the summary financial statements are derived.

4.2.1 Before accepting an engagement to report on summary financial statements, the auditor shall:

(a) Determine whether the applied criteria are acceptable.

Applied criteria refer to the criteria applied by management in the preparation of the summary financial statements. Management is responsible for the determination of the information that needs to be reflected in the summary financial statements so that they are consistent, in all material respects, with or represent a fair summary of the audited financial statements.

Factors affecting the auditor's determination of the acceptability of the applied criteria:

- The nature of the entity
- The purpose of the summary financial statements
- The information needs of the intended users of the summary financial statements and
- Whether the applied criteria will result in summary financial statements that are not misleading in the circumstances.

If the auditor concludes that the applied criteria are unacceptable or is unable to obtain the agreement of management as discussed above, the auditor shall not accept the engagement to report on the summary financial statements, unless required by law or regulation to do so. An engagement conducted in accordance with such law or regulation does not comply with this SA. Accordingly, the auditor's report on the summary financial statements shall not indicate that the engagement was conducted in accordance with this SA.

(b) Obtain the agreement of management that it acknowledges and understands its responsibility:

(i) For the preparation of the summary financial statements in accordance with the applied criteria.

(ii) To make the audited financial statements available to the intended users of the summary financial statements without undue difficulty.

The auditor's evaluation whether the audited financial statements are available to the intended users of the summary financial statements without undue difficulty is affected by factors such as whether:
• The summary financial statements describe clearly from whom or where the audited financial statements are available

- *The audited financial statements are on public record; or*
- *Management has established a process by which the intended users of the summary financial statements can obtain ready access to the audited financial statements*

(iii) *To include the auditor's report on the summary financial statements in any document that contains the summary financial statements and that indicates that the auditor has reported on them*

(c) *Agree with management on the form of opinion to be expressed on the summary financial statements.*

4.3 Nature of Procedures to be performed by Auditor

(a) *Evaluate whether the summary financial statements adequately disclose the summarised nature and identify the audited financial statements.*

(b) *When summary financial statements are not accompanied by the audited financial statements, evaluate whether they describe clearly:*

(i) *From whom or where the audited financial statements are available; or*

(ii) *The law or regulation that specifies that the audited financial statements need not be made available to the intended users of the summary financial statements and establishes the criteria for the preparation of the summary financial statements.*

(c) *Evaluate whether the summary financial statements adequately disclose applied criteria.*

(d) *Compare the summary financial statements with the related information in audited financial statements to determine whether the summary financial statements agree with or can be re-calculated from the related information in the audited financial statements.*

(e) *Evaluate whether the summary financial statements are prepared in accordance with the applied criteria.*

(f) *Evaluate, in view of the purpose of the summary financial statements, whether summary financial statements contain the information necessary, and are at an appropriate level of aggregation, so as not to be misleading in the circumstances.*

(g) *Evaluate whether the audited financial statements are available to the intended users of the summary financial statements without undue difficulty.*

4.4 Form of Opinion

When the auditor has concluded that an unmodified opinion on the summary financial statements is appropriate, the auditor's opinion shall, unless otherwise required by law or regulation, use one of the following phrases:

(a) The summary financial statements are consistent, in all material respects, with the audited financial statements, in accordance with the applied criteria or

(b) The summary financial statements are a fair summary of the audited financial statements, in accordance with the applied criteria

If law or regulation prescribes the wording of the opinion on summary financial statements in terms that are different from those described above, the auditor shall:

(a) Apply the procedures discussed earlier and any further procedures necessary to enable the auditor to express the prescribed opinion and

(b) Evaluate whether users of the summary financial statements might misunderstand the auditor's opinion on the summary financial statements and, if so, whether additional explanation in the auditor's report on the summary financial statements can mitigate possible misunderstanding.

If, the auditor concludes that additional explanation in the auditor's report on the summary financial statements cannot mitigate possible misunderstanding, the auditor shall not accept the engagement, unless required by law or regulation to do so. An engagement conducted in accordance with such law or regulation does not comply with this SA. Accordingly, the auditor's report on the summary financial statements shall not indicate that the engagement was conducted in accordance with this SA.

4.5 Auditor's Report on Summary Financial Statements

(a) A title clearly indicating it as the report of an independent auditor

(b) **An addressee:** If the addressee of the summary financial statements is not the same as the addressee of the auditor's report on the audited financial statements, the auditor shall evaluate the appropriateness of using a different addressee.

(c) An introductory paragraph:

An Introductory Paragraph	(i) Identifies the summary financial statements on which the auditor is reporting, including the title of each statement included in the summary financial statements.
	(ii) Identifies the audited financial statements
	(iii) Refers to the auditor's report on the audited financial statements, the date of that report, and, in cases other than where audited financial statements contain modified opinion, emphasis of matter paragraph and other matter paragraph, the fact that an unmodified opinion is expressed on the audited financial statements;
	(iv) If the date of the auditor's report on the summary financial statements is later than the date of the auditor's report on the audited financial statements, states that the summary financial statements and the audited financial statements do not reflect the effects of events that occurred subsequent to the date of the auditor's report on the audited financial statements; and
	(v) A statement indicating that the summary financial statement do not contain all the disclosures required by the financial reporting frame work applied in the preparation of the audited financial statements, and that reading the summary financial statements is not a substitute for reading the audited financial statements.

(d) A description of management's responsibility for the summary financial statement.

(e) A statement that the auditor is responsible for expressing an opinion on the summary financial statements based on the procedures required by this SA.

(f) A paragraph clearly expressing an opinion.

(g) The auditor's signature along with the firm registration number, wherever applicable, and the membership number assigned by the Institute of Chartered Accountants of India. Besides, UDIN is required to be stated.

(h) The date of the auditor's report

The auditor shall date the auditor's report on the summary financial statements no earlier than:

(i) The date on which the auditor has obtained sufficient appropriate evidence; and

(ii) The date of the auditor's report on the audited financial statements.

(i) The place of signature.

4.6 Modifications to the Opinion, Emphasis of Matter Paragraph or Other Matter Paragraph in the Auditor's Report on the Audited Financial Statements

When the auditor's report on the audited financial statements contains a qualified opinion, an Emphasis of Matter paragraph, or an Other Matter paragraph, but the auditor is satisfied that the summary financial statements are consistent, in all material respects, with or are a fair summary of the audited financial statements, in accordance with the applied criteria, the auditor's report on the summary financial statements shall, also contain followings:-

(a) State that the auditor's report on the audited financial statements contains a qualified opinion, an Emphasis of Matter paragraph, or an Other Matter paragraph; and

(b) Describe:

(i) The basis for the qualified opinion on the audited financial statements, and that qualified opinion; or the Emphasis of Matter or the Other Matter paragraph in the auditor's report on the audited financial statements; and

(ii) The effect thereof on the summary financial statements, if any.

When the auditor's report on the audited financial statements contains an adverse opinion or a disclaimer of opinion, the auditor's report on the summary financial statements shall, additionally: -

(a) State that the auditor's report on the audited financial statements contains an adverse opinion or disclaimer of opinion;

(b) Describe the basis for that adverse opinion or disclaimer of opinion; and

(c) State that, as a result of the adverse opinion or disclaimer of opinion, it is inappropriate to express an opinion on the summary financial statements.

4.6.1 Modified Opinion on the Summary Financial Statements

If the summary financial statements are not consistent, in all material respects, with or are not a fair summary of the audited financial statements, in accordance with the applied criteria, and management does not agree to make the necessary changes, the auditor shall express an adverse opinion on the summary financial statements.

4.7 Restriction on Distribution or Use or Alerting Readers to the Basis of Accounting

When distribution or use of the auditor's report on the audited financial statements is restricted, or the auditor's report on the audited financial statements alerts readers that the audited financial statements are prepared in accordance with a special purpose framework, the auditor shall include a similar restriction or alert in the auditor's report on the summary financial statements.

4.8. Comparatives

If the audited financial statements contain comparatives, but the summary financial statements do not, the auditor shall determine whether such omission is reasonable in the circumstances of the engagement.

The auditor shall determine the effect of an unreasonable omission on the auditor's report on the summary financial statements.

4.9 Unaudited Supplementary Information Presented With Summary Financial Statements

Similar to SA 700 chapter 7

4.10 Other Information in Documents Containing Summary Financial Statements

Similar to SA 720 chapter 7

4.11 Auditor Association

If the auditor becomes aware that the entity plans to state that the auditor has reported on summary financial statements in a document containing the summary financial statements, but does not plan to include the related auditor's report, the auditor shall request management to include the auditor's report in the document. If management does not do so, the auditor shall determine and carry out other appropriate actions designed to prevent management from inappropriately associating the auditor with the summary financial statements in that document.

The auditor maybe engaged to report on the financial statements of an entity, while engaged to report on the summary financial statements. If, in this case, the auditor becomes aware that the entity plans to make a statement in a document that refers to the auditor and the fact that summary financial statements are

derived from the financial statements audited by the auditor, the auditor shall be satisfied that:
(a) The reference to the auditor is made in the context of the auditor's report on the audited financial statements; and
(b) The statement does not give the impression that the auditor has reported on the summary financial statements.

If (a) or (b) are not met, the auditor shall request management to change the statement to meet them, or not to refer to the auditor in the document. Alternatively, the entity may engage the auditor to report on the summary financial statements and include the related auditor's report in the document. If management does not change the statement, delete the reference to the auditor, or include an auditor's report on the summary financial statements in the document containing the summary financial statements, the auditor shall advise management that the auditor disagrees with the reference to the auditor, and the auditor shall determine and carry out other appropriate actions designed to prevent management from inappropriately referring to the auditor.

4.12 Timing of Work and Events Subsequent to the Date of the Auditor's Report on the Audited Financial Statements

When the auditor reports on the summary financial statements after the completion of the audit of the financial statements, the auditor is not required to obtain additional audit evidence on the audited financial statements, or report on the effects of events that occurred subsequent to the date of the auditor's report on the audited financial statements since the summary financial statements are derived from the audited financial statements.

9. AUDIT - RELATED SERVICES

1. INTRODUCTION

What are Related Services?

Not all engagements performed by practitioners are assurance engagements. Other frequently performed engagements that do not meet the definition of assurance engagements include:-

- The preparation of tax returns where no conclusion conveying assurance is expressed.
- Consulting (or advisory) engagements such as management and tax consulting.
- Engagements covered by Standards for Related Services, such as agreed-upon procedures engagements and compilations of financial or other information.

The above engagements are in nature of related services.

2. SRS 4400 ENGAGEMENTS TO PERFORM AGREED-UPON PROCEDURES REGARDING FINANCIAL INFORMATION

2.1 Objective in Accordance with SRS 4400

The objective of an agreed-upon procedures engagement is for the auditor to carry out procedures of an audit nature to which the auditor and the entity and any appropriate third parties have agreed and to report on factual findings.

The report is usually restricted to those parties that have agreed to the procedures to be performed since others, unaware of the reasons for the procedures, may misinterpret the results.

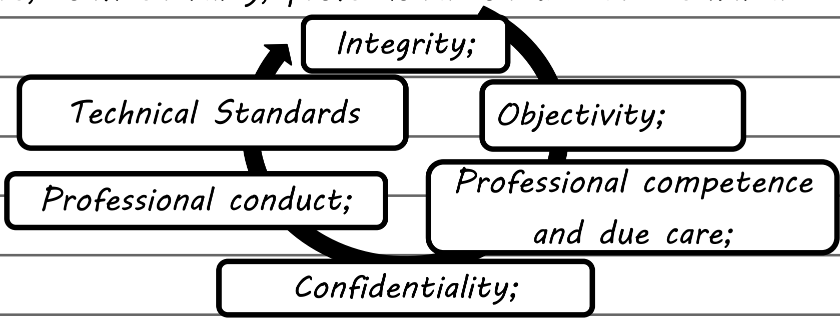
2.2 Audit Vs. Agreed-upon Procedures

A key difference between an audit and agreed-upon procedures relates to assurance. An audit expresses an opinion and provides assurance to users. However, in an agreed-procedures engagement, only a report of the factual findings of agreed-upon procedures is provided. No assurance is given to users. Instead, users draw their own conclusions based on factual findings stated in the report.

2.3 General Principles of an Agreed-upon Procedures Engagement

The auditor should comply with the Code of Ethics, issued by the Institute of Chartered

Accountants of India. Ethical principles governing the auditor's professional responsibilities for this type of engagement include integrity, objectivity, professional competence and due care, confidentiality, professional conduct and technical standards.



Independence is not a requirement for agreed-upon procedures engagement. Where the auditor is not independent, a statement to that effect should be made in the report of factual findings.

2.3.1 Defining the Terms of the Engagement

The auditor should ensure with representatives of the entity and, ordinarily, other specified parties who will receive copies of the report of factual findings, that there is a clear understanding regarding the agreed procedures and the conditions of the engagement.

Matters to be agreed include the following:-

(a) Nature of the engagement including the fact that the procedures performed will not constitute an audit or a review and that accordingly no assurance will be expressed.

(b) Stated purpose for the engagement.

(c) Identification of the financial information to which the agreed-upon procedures will be applied.

(d) Nature, timing and extent of the specific procedures to be applied.

(e) Limitations on distribution of the report of factual findings. When such limitation would be in conflict with the legal requirements, if any, the auditor would not accept the engagement.

2.3.2 Planning

The auditor should plan the work so that an effective engagement will be performed.

2.3.3 Procedures and Evidence

The auditor should carry out the procedures agreed-upon and use the evidence obtained as the basis for the report of factual findings.

The procedures applied in an engagement to perform agreed - upon procedures may include:

- Inquiry and analysis
- Re computation, comparison and other clerical accuracy checks
- Observation
- Inspection
- Obtaining confirmations

2.4 Reporting

The report of factual findings should contain:
(a) Title
(b) Addressee (ordinarily, the appointing authority)
(c) Identification of specific financial or non-financial information to which the agreed upon procedures have been applied
(d) A statement that the procedures performed were those agreed-upon with the recipient
(e) A statement that the engagement was performed in accordance with the Standard Related Services applicable to agreed-upon procedures engagements
(f) Identification of the purpose for which the agreed-upon procedures were performed
(g) A listing of the specific procedures performed
(h) A description of the auditor's factual findings including sufficient details of errors an exceptions found
(i) A statement that the procedures performed do not constitute either an audit or a review and, as such, no assurance is expressed
(j) A statement that had the auditor performed additional procedures, an audit or a review, other matters might have come to light that would have been reported
(k) A statement that the report is restricted to those parties that have agreed to procedures to be performed
(l) A statement (when applicable) that the report relates only to the elements, accounts, items or financial and non-financial information specified and that it does not extend the entity's financial statements taken as a whole
(m) Date of the report
(n) Place of signature and
(o) Auditor's signature

3. SRS 4410 COMPILATION ENGAGEMENTS

Management may request a professional accountant in public practice to assist with the preparation and presentation of financial information of an entity.

❖ **Financial information that is the subject of a compilation engagement may be required for various purposes including-:**

1. **To comply with mandatory periodic financial reporting requirements established in law or regulation, if any or**
2. **For purposes unrelated to mandatory financial reporting under relevant law or regulation, including for example:**

- For management or those charged with governance, prepared on a basis appropriate for their particular purposes (such as preparation of financial information for internal use).
- For periodic financial reporting undertaken for external parties under a contract or other form of agreement (such as financial information provided to a funding body to support provision or continuation of a grant).
- For transactional purposes, for example to support a transaction involving changes to the entity's ownership or financing structure (such as for a merger or acquisition).

3.1 Objectives in accordance with SRS 4410

The practitioner's objectives in a compilation engagement under this SRS are to: -

Objectives in a Compilation Engagement to:-

(a) Apply accounting and financial reporting expertise to assist management in the preparation and presentation of financial information in accordance with an applicable financial reporting framework based on information provided by management and

(b) Report in accordance with the requirements of this SRS.

3.2 Scope of Compilation Engagements

The scope of a compilation engagement will vary depending on the circumstances of the engagement.

Management retains responsibility for the financial information and the basis on which

it is prepared and presented. That responsibility includes application by management of the judgment required for the preparation and presentation of the financial information, including the selection and application of appropriate accounting policies and, where needed, developing reasonable accounting estimates.

3.3 Ethical Requirements

Similar to point 2.3 of this chapter

3.4 Engagement Acceptance and Continuance

The practitioner shall not accept the engagement unless the practitioner has agreed the terms of engagement with management, & the engaging party if different, including:-

(a) The intended use and distribution of the financial information, and any restrictions on either its use or its distribution where applicable

(b) Identification of the applicable financial reporting framework

(c) The objective and scope of the compilation engagement

(d) The responsibilities of the practitioner, including the requirement to comply with relevant ethical requirements

(e) The responsibilities of management for: -

The responsibilities of management for

(i)	(ii)	(iii)	(iv)
The financial information, and for the preparation & presentation thereof, in accordance with a financial reporting framework that is acceptable in view of the intended use of the financial information & the intended users	Design, implementation and maintenance of such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error	The accuracy and completeness of the records, documents, explanations and other information provided by management for the compilation engagement and	Judgments needed in the preparation and presentation of the financial information, including those for which the practitioner may provide assistance in the course of the compilation engagement

(f) The expected form and content of the practitioner's report.

3.5 Performing the Engagement

- The practitioner shall **obtain an understanding** of the following matters sufficient to be able to perform the compilation engagement:-

(a) The entity's business and operations, and

(b) The applicable financial reporting framework

- The practitioner shall **compile the financial information** using the records, documents, explanations & other information, including significant judgments, provided by management.
- The practitioner shall **discuss with management, or those charged with governance** as appropriate, those significant judgments, for which the practitioner has provided assistance in the course of compiling the financial information.
- Prior to completion of the compilation engagement, the practitioner shall **read the compiled financial information in light of the practitioner's understanding of the entity's business and operations, and of the applicable financial reporting framework.**
- If, in the course of the compilation engagement, the practitioner becomes aware that the records, documents, explanations or other information, including significant judgments, provided by management for the compilation engagement are incomplete, inaccurate or otherwise unsatisfactory, the practitioner shall bring that to the attention of management and request the additional or corrected information.
- If the practitioner is **unable to complete the engagement** because management has failed to provide records, documents, explanations or other information, including significant judgments, as requested, the practitioner shall withdraw from the engagement and inform management and those charged with governance of the reasons for withdrawing.
- If the practitioner becomes aware during the course of the engagement that:-

(a) The compiled financial information does not adequately refer to or describe the applicable financial reporting framework

(b) Amendments to the compiled financial information are required for the financial information not to be materially misstated; or

(c) The compiled financial information is otherwise misleading, the practitioner shall propose the appropriate amendments to management.

- If management declines, or does not permit the practitioner to make the proposed amendments to the compiled financial information, the practitioner shall withdraw from the engagement and inform management and those charged with governance of the reasons for withdrawing.

- If withdrawal from the engagement is not possible, the practitioner shall determine the professional and legal responsibilities applicable in the circumstances.
- The practitioner shall obtain an acknowledgement from management or those charged with governance, as appropriate, that they have taken responsibility for the final version of the compiled financial information.

3.6 Communication with Management and Those Charged with Governance

The practitioner shall communicate with management or those charged with governance, as appropriate, on a timely basis during the course of the compilation engagement, all matters concerning the compilation engagement that, in the practitioner's professional judgment, are of sufficient importance to merit the attention of management or those charged with governance, as appropriate.

3.7 The Practitioner's Report

The practitioner's report issued for the compilation engagement shall be in writing, and include the following elements: -
(a) The report title
(b) The addressee(s), as required by the terms of the engagement
(c) A statement that the practitioner has compiled the financial information based on information provided by management
(d) A description of the responsibilities of management.
(e) Identification of the applicable financial reporting framework.
(f) Identification of the financial information, including the title of each element of the financial information if it comprises more than one element, and the date of the financial information or the period to which it relates
(g) A description of the practitioner's responsibilities in compiling the financial information, including that the engagement was performed in accordance with this SRS, and that the practitioner has complied with relevant ethical requirements
(h) A description of what a compilation engagement entails in accordance with this SRS

(i) Explanations that: -
• *Since a compilation engagement is not an assurance engagement, the practitioner is not required to verify the accuracy or completeness of the information provided by management for the compilation and*
• *Accordingly, the practitioner does not express an audit opinion or a review conclusion on whether the financial information is prepared in accordance with the applicable financial reporting framework.*
(j) If the financial information is prepared using a special purpose financial reporting framework, an explanatory paragraph that: -
• *Describes the purpose for which the financial information is prepared and, if necessary, the intended users, or contains a reference to a note in the financial information that discloses this information and*
• *Draws the attention of readers of the report to the fact that the financial information is prepared in accordance with a special purpose framework and that, as a result, the information may not be suitable for other purposes*
(k) The date of the practitioner's report
(l) The practitioner's signature and
(m) The place of signature.

3.8 Engagement Level Quality Control

The engagement partner shall take responsibility for: -

(a) The overall quality of each compilation engagement to which that partner is assigned and

(b) The engagement being performed in accordance with the firm's quality control policies and procedures

10. REVIEW OF FINANCIAL INFORMATION

1. INTRODUCTION

What is REVIEW?

"Review" is a limited assurance engagement Limited assurance is the level of assurance obtained where engagement risk is reduced to a level that is acceptable in the circumstances of the engagement, but where that risk is greater than for a reasonable assurance engagement, as the basis for expressing a conclusion. The combination of the nature, timing and extent of evidence gathering procedures is at least sufficient for the practitioner to obtain a meaningful level of assurance. To be meaningful, the level of assurance obtained by the practitioner is likely to enhance the intended users' confidence about the financial statements.

2. SRE 2400 ENGAGEMENTS TO REVIEW HISTORICAL FINANCIAL STATEMENTS

2.1 Objectives in a review of financial statements in accordance with SRE 2400

(a) Obtain limited assurance, primarily by making an inquiry and performing analytical procedures

(b) Report on the financial statements as a whole and communicate, as required by this SRE.

In all cases when limited assurance cannot be obtained and a modified conclusion in the practitioner's report is insufficient in the circumstances, this SRE requires that the practitioner either to disclaim a conclusion in the report issued for the engagement or, where appropriate to withdraw from the engagement if withdrawal is possible under applicable law or regulations.

2.2 Compliance with Ethical Requirements and Engagement Level Quality Control

The practitioner shall comply with relevant ethical requirements, including those pertaining to independence and the engagement partner is responsible for overall quality of each review engagement.

Factors affecting Acceptance and Continuance of Client Relationships and Review Engagements:

Unless required by law or regulation, the practitioner shall not accept a review engage if:

(a) The practitioner is not satisfied:

(i) That there is a rational purpose for the engagement.

(ii) That a review engagement would be appropriate in the circumstances.

(b) The practitioner has reason to believe that relevant ethical requirements, including independence, will not be satisfied.

(c) The practitioner's preliminary understanding of the engagement circumstances indicates that information needed to perform the review engagement is likely to be unavailable or unreliable.

(d) The practitioner has cause to doubt management's integrity such that it is likely to affect proper performance of the review or

(e) Management or those charged with governance impose a limitation on the scope

2.3 Preconditions for Accepting a Review Engagement

Prior to accepting a review engagement, the practitioner shall: -

(a) Determine whether the financial reporting framework applied in the preparation of the financial statements is acceptable and;

(b) Obtain the agreement of management that it acknowledges & understands its responsibilities:

(i) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including, where relevant, their fair presentation.

(ii) For such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and

(iii) To provide the practitioner with: -

(a) Access to all information of which management is aware that is relevant to the preparation of the financial statements

(b) Additional information that the practitioner may request and

(c) Unrestricted access to persons within the entity

If the practitioner is not satisfied as to any of the matters set out above as preconditions for accepting a review engagement, the practitioner shall discuss the matter with the management or those charged with governance.

If changes cannot be made to satisfy the practitioner as to those matters, the practitioner shall not accept the proposed engagement unless required by law or regulation to do so. However, an engagement conducted under such circumstances does not comply with this SRE. Accordingly, the practitioner shall not include any reference within the practitioner's report to the review having been conducted in accordance with this SRE.

If it is discovered after the engagement has been accepted that the practitioner is not satisfied as to any of the above preconditions, the practitioner shall discuss the matter with the management or those charged with governance and shall determine:

(a) Whether the matter can be resolved

(b) Whether it is appropriate to continue with the engagement and

(c) Whether and, if so, how to communicate the matter in the practitioner's report.

2.4. Agreeing to the Terms of Engagement

The agreed terms of engagement shall be recorded in an engagement letter or other suitable form of written agreement. On recurring review engagements, the practitioner shall evaluate whether circumstances, including changes in the engagement acceptance considerations, require the terms of engagement to be revised and whether there is a need to remind management or those charged with governance, as appropriate, of the existing terms of engagement.

Overview of performing the review engagement after its acceptance in accordance with SRE 2400

- Determine materiality for financial statements as a whole
- Obtain understanding of entity and applicable financial reporting framework to identify areas of possible material misstatements
- Design and perform "inquiry" and "Analytical procedures"
- Perform procedures to address specific circumstances
- Perform other procedures, if necessary, in circumstances

(i) Materiality in a Review of Financial Statements

The practitioner shall determine materiality for the financial statements as a whole and apply this materiality in designing the procedures and in evaluating the results obtained from those procedures. The practitioner's judgment about what is material in relation to the financial statements as a whole is the same regardless of the level of assurance obtained by a practitioner as the basis for expressing the conclusion on the financial statements.

The practitioner shall revise materiality for the financial statements as a whole in the event of becoming aware of any information during the review that would have caused the practitioner to have determined a different amount initially.

(ii) Obtaining Understanding of the Entity

The practitioner shall obtain an understanding of the entity and its environment and the applicable financial reporting framework to identify areas in the financial statements where material misstatements are likely to arise and thereby provide a basis for designing procedures to address those areas.

(iii) Designing and Performing Procedures

In obtaining sufficient appropriate evidence as the basis for a conclusion on the financial statements as a whole, the practitioner shall design and perform inquiry and analytical procedures:-

(a) To address all material items in the financial statements, including disclosures and

(b) To focus on addressing areas in the financial statements where material misstatements are likely to arise.

(a) **Inquiry:** In a review, inquiry includes seeking information from management and other persons within the entity, as the practitioner considers appropriate in the engagement circumstances.

Inquiries may include matters such as those relating to making of accounting estimates, identification of related parties, about significant, complex or unusual transactions, existence of any actual, suspected or alleged fraud, events occurring between the date of the financial statements and practitioner's report, basis for management's assessment of the entity's ability to continue as a going concern, events or conditions that appear to cast doubt on the entity's ability to continue as a going concern, material commitments, contractual obligations or contingencies that have affected or may affect the entity's financial statements including disclosures and material non-monetary transactions or transactions for no consideration in the financial reporting period under consideration.

The practitioner may also extend Inquiries to obtain non-financial data if appropriate. Evaluating the responses provided by the management is integral to the inquiry process.

Depending on the engagement circumstances, inquiries may also include inquiries about:

- Actions taken at meetings of owners, those charged with governance and committees.
- Communications the entity has received, or expects to receive or obtain, from regulatory agencies.
- Matters arising in the course of applying other procedures.

(b) **Analytical procedures:** In designing analytical procedures, the practitioner shall consider whether the data from the entity's accounting system and accounting records are adequate for the purpose of performing the analytical procedures.

Why "Inquiry" and "Analytical procedures" are important in Review?

Evidence obtained through inquiry is often the principal source of evidence about management intent. However, information available to support management's intent may be limited. In that case, understanding management's past history of carrying out its stated intentions, management's stated reasons for choosing a particular course of action, and management's ability to pursue a specific course of action may provide relevant information to corroborate the evidence obtained through inquiry. Application of professional scepticism in evaluating responses provided by management is important to enable the practitioner to evaluate whether there are any matters that would cause the practitioner to believe the financial statements may be materially misstated.

In a review of financial statements, performing analytical procedures assists the practitioner in:

- *Obtaining or updating the practitioner's understanding of the entity & its environment*
- *Identifying inconsistencies or variances*
- *Providing corroborative evidence*
- *Serving as additional procedures when the practitioner becomes aware of matters that cause the practitioner to believe that the financial statements may be materially misstated.*

(iv) Procedures to Address Specific Circumstances

- ***Related parties:*** *During the review, the practitioner shall remain alert for arrangements or information that may indicate the existence of related party relationships or transactions that the management has not previously identified or disclosed to the practitioner. If the practitioner identifies significant transactions outside the entity's normal course of business during the course of review, the practitioner shall inquire with the management about the nature of those transactions, possible involvement of related parties and the business rationale (or lack thereof) of those transactions.*

- ***Fraud and non-compliance with laws or regulations:*** *When there is an indication that fraud or non-compliance with laws or regulations, or suspected fraud or non-compliance with laws or regulations, has occurred in the entity, the practitioner shall communicate that matter to the appropriate level of senior management or those charged with governance as appropriate and request management's assessment of the effects, if any, on the financial statements.*

- ***Going concern:*** *If, during the performance of the review, the practitioner becomes aware of events or conditions that may cast significant doubt about the entity's ability to continue as a going concern, the practitioner shall:*

(a) *Inquire of management about plans for future actions affecting the entity's ability to continue as a going concern and about the feasibility of those plans*

(b) Evaluate the results of those inquiries, to consider whether management's responses provide a sufficient basis to: -

(i) Continue to present the financial statements on the going concern basis

(ii) Conclude whether the financial statements are materially misstated, or are otherwise misleading regarding the entity's ability to continue as a going concern and

(c) Consider management's responses

♦ **Use of work performed by others:** In performing the review, it may be necessary for the practitioner to use work performed by other practitioners, or the work of an individual or organization possessing expertise in a field other than accounting or assurance. If the practitioner uses work performed by another practitioner or an expert in the course of performing the review, the practitioner shall take appropriate steps to be satisfied that the work performed is adequate for the practitioner's purposes.

(v) Additional procedures when the practitioner becomes aware that the financial statements may be materially misstated:

(a) Conclude that the matter(s) is not likely to cause the financial statements as a whole to be materially misstated or

(b) Determine that the matter(s) causes the financial statements as a whole to be materially misstated.

Additional procedures focus on obtaining sufficient appropriate evidence to enable the practitioner to form a conclusion on matters that the practitioner believes may cause the financial statements to be materially misstated. The procedures may be:

♦ Additional inquiry or analytical procedures, for example, being performed in greater detail or being focused on the affected items (i.e. amounts or disclosures concerning the affected accounts or transactions as reflected in the financial statements); or

♦ Other types of procedures, for example, substantive test of details or external confirmations.

The practitioner has no obligation to perform any procedures regarding the financial statements after the date of the practitioner's report. However, if, after the date of the practitioner's report but before the date the financial statements are issued, a fact becomes known to the practitioner that, had it been known to the practitioner at the date of the practitioner's report, may have caused the practitioner to amend the report, the practitioner shall:-

Similar to SA 560 chapter 6

(vi) **Written Representations**

Written representations are an important source of evidence in a review engagement. If management modifies or does not provide the requested written representations, it may alert the practitioner to the possibility that one or more significant issues may exist. Further, a request for written, rather than oral, representations in many cases may prompt management to consider such matters more rigorously, thereby enhancing the quality of the representations.

The practitioner shall request management to provide written representation that management has fulfilled its responsibilities described in the agreed terms of engage the written representation shall include that:

(a) Management has fulfilled its responsibility for the preparation of financial statements and

(b) All transactions have been recorded and are reflected in the financial statements.

If law or regulation requires management to make written public statements about its responsibilities, and the practitioner determines that such statements provide some or all of the representations required above, the relevant matters covered by such statements need not be included in the written representation.

The practitioner shall also request management's written representations management has disclosed to the practitioner:-

(a) The identity of the entity's related parties and all the related party relationships and transactions of which management is aware;

(b) Significant facts relating to any frauds or suspected frauds known to management that may have affected the entity;

(c) Known actual or possible non-compliance with laws and regulations for which the effects of non-compliance affect the entity's financial statements;

(d) All information relevant to use of the going concern assumption in the financial statements;

(e) That all events occurring subsequent to the date of the financial statements and for which the applicable financial reporting framework requires adjustment or disclosure, have been adjusted or disclosed;

(f) Material commitments, contractual obligations or contingencies that have affected or may affect the entity's financial statements, including disclosures;

(g) Material non-monetary transactions or transactions for no consideration undertaken by the entity in the financial reporting period under consideration.

If management does not provide one or more of the requested written representations, the practitioner shall:-

(a) Discuss the matter with management and those charged with governance, as appropriate;

(b) Re-evaluate the integrity of management, and evaluate the effect that this may have on the reliability of representations (oral or written) and evidence in general; and

(c) Take appropriate actions, including determining the possible effect on the conclusion in the practitioner's report in accordance with this SRE.

The practitioner shall disclaim a conclusion on the financial statements, or withdraw from the engagement if withdrawal is possible under applicable law or regulation, as appropriate, if: -

(a) The practitioner concludes that there is sufficient doubt about the integrity of management such that the written representations are not reliable or

(b) Management does not provide the required representations in respect of its responsibilities for preparation of financial statements and recording of all transactions in financial statements.

Evaluating evidence obtained from the procedures performed

The practitioner considers that the evidence obtained from the procedures performed is not sufficient and appropriate to be able to form a conclusion on the financial statements.

The practitioner may:

- Extend the work performed or
- Perform other procedures judged by the practitioner to be necessary in the circumstances.

(viii) Forming the practitioner's conclusion on the financial statements

In forming conclusion, the practitioner shall also consider the impact of: -

(a) Uncorrected misstatements identified during the review, and in the previous year's review of the entity's financial statements, on the financial statements as a whole

(b) Qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgments.

Unmodified Conclusion: The practitioner shall express an unmodified conclusion in the practitioner's report on the financial statements as a whole when the practitioner has obtained limited assurance to be able to conclude that nothing has come to the practitioner's attention that causes the practitioner to believe that the financial statements are not prepared, in all material respects, in accordance with the applicable financial reporting framework.

Modified Conclusion: The practitioner shall express a modified conclusion in the practitioner's report on the financial statements as a whole when:

(a) The practitioner determines, based on the procedures performed and the evidence obtained, that the financial statements are materially misstated or

(b) The practitioner is unable to obtain sufficient and appropriate evidence in relation to one or more items in the financial statements that are material in relation to the financial statements as a whole.

When the practitioner modifies the conclusion expressed on the financial statements, the practitioner shall:

(a) Use the heading "Qualified Conclusion," "Adverse Conclusion" or "Disclaimer of Conclusion," as appropriate, for the conclusion paragraph in the practitioner's report and

(b) Provide a description of the matter giving rise to the modification, under an appropriate heading (for example, "Basis for Qualified Conclusion," "Basis for Adverse Conclusion" or "Basis for Disclaimer of Conclusion," as appropriate) in a separate paragraph in the practitioner's report immediately before the conclusion paragraph (referred to as the basis for conclusion paragraph).

In the basis for conclusion paragraph, in relation to material misstatements that give rise to either a qualified conclusion or an adverse conclusion, the practitioner shall:-

(a) Describe and quantify the financial effects of the misstatement if the material Misstatement relates to specific amounts in the financial statements (including quantitative disclosures), unless impracticable, in which case the practitioner shall so state;

(b) Explain how disclosures are misstated if the material misstatement relates to narrative disclosures; or

(c) Describe the nature of omitted information if the material misstatement relates to the non- disclosure of information required to be disclosed. Unless prohibited by law or regulation, the practitioner shall include the omitted disclosures where practicable to do so.

The practitioner shall withdraw from the engagement if the following conditions are present-:

(a) Due to a limitation on the scope of the review imposed by management after the practitioner has accepted the engagement, the practitioner is unable to obtain sufficient appropriate and evidence to form a conclusion on the financial statements;

(b) The practitioner has determined that the possible effects on the financial statements of undetected misstatements are material and pervasive and

(c) Withdrawal is possible under applicable law or regulation.

In the basis for conclusion paragraph, in relation to either the qualified conclusion due to inability of obtaining sufficient and appropriate evidence or when the practitioner disclaims a conclusion, the practitioner shall include the reason(s) for the inability to obtain sufficient and appropriate evidence.

(ix) The Practitioner's Report

(a) A title, which shall clearly indicate that it is the report of an independent practitioner for a review engagement

(b) The addressee(s), as required by the circumstances of the engagement

(c) An introductory paragraph that:

(1) Identifies the financial statements reviewed, including identification of the title of each of the statements contained in the set of financial statements and the date and period covered by each financial statement

(2) Refers to the summary of significant accounting policies

(3) States that the financial statements have been reviewed

(d) A description of the responsibility of management

(1) Their preparation in accordance with the applicable financial reporting framework including, where relevant, their fair presentation;

(2) Such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error;

(e) If the financial statements are special purpose financial statements:

(1) A description of the purpose for which the financial statements are prepared

(2) If management has a choice of financial reporting frameworks in the preparation of such financial statements, a reference within the explanation of management's responsibility for the financial statements to management's responsibility for determining that the applicable financial reporting framework is acceptable in the circumstances

(f) A description of the practitioner's responsibility to express a conclusion on the

financial statements including reference to this SRE and, where relevant, applicable law or regulation.

(g) A description of a review of financial statements and its limitations, and following statements:

(1) *A review engagement under this SRE is a limited assurance engagement.*

(2) *The practitioner performs procedures, primarily consisting of making inquiries of management and others within the entity, as appropriate, and applying analytical procedures, and evaluates the evidence obtained and*

(3) *The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with Standards on Auditing (SAs), and, accordingly, the practitioner does not express an audit opinion on the financial statements.*

(h) A paragraph under the heading "Conclusion" that contains:

(1) *The practitioner's conclusion on the financial statements as a whole as appropriate and*

(2) *A reference to the applicable financial reporting framework used to prepare the financial statements.*

(i) When the practitioner's conclusion on the financial statements is modified:

(1) *A paragraph under the appropriate heading that contains the practitioner's modified conclusion as appropriate and*

(2) *A paragraph, under an appropriate heading, that provides a description of the matter(s) giving rise to the modification*

(j) *A reference to the practitioner's obligation under this SRE to comply with relevant ethical requirements*

(k) The date of the practitioner's report: *The practitioner shall date the report no earlier than the date on which the practitioner has obtained sufficient appropriate evidence as the basis for the practitioner's conclusion on the financial statements, including being satisfied that: -*

(1) *All the statements that comprise the financial statements under the applicable financial reporting framework, including the related notes where applicable, have been prepared and*

(2) *Those with the recognized authority have asserted that they have taken responsibility for those financial statements.*

(l) The practitioner's signature and

(m) The place of signature.

2.5 Emphasis of Matter and Other Matter Paragraphs in the Practitioner's Report

Similar to SA 706 Chapter 7

2.6 Other Reporting Responsibilities

Similar to SA 700 Chapter 7

2.7 Documentation

The practitioner shall document the following aspects of the engagement in a timely manner, sufficient to enable an experienced practitioner, having no previous connection with the engagement, to understand:

(a) The nature, timing, and extent of the procedures performed to comply with this SRE and applicable legal and regulatory requirements

(b) Results obtained from the procedures, and the practitioner's conclusions formed on the basis of those results and

(c) Significant matters arising during the engagement, the practitioner's conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

While documenting the nature, timing and extent of procedures performed as required in this SRE, the practitioner shall record:

(a) Who performed the work and the date such work was completed and

(b) Who reviewed the work performed for the purpose of quality control for the engagement, and the period and extent of the review.

(d) If, in the course of the engagement, the practitioner identified information that is inconsistent with the practitioner's findings regarding significant matters affecting the financial statements, the practitioner shall document how the inconsistency was addressed.

2.8 Audit Vs. Review

Overview of distinctive areas between Audit and Review

Audit	Review
Audit is a type of reasonable assurance engagement providing reasonable level of assurance.	Review is a type of limited assurance engagement providing a lower level of assurance than reasonable assurance engagement.
It performs elaborate and extensive procedures including tests of controls and substantive procedures.	It performs fewer procedures primarily focusing on inquiry and analytical procedures.
It draws reasonable conclusions on the basis of sufficient appropriate evidence.	It draws limited conclusions on the basis of sufficient appropriate evidence.
It provides an assurance opinion. The language of assurance opinion is positively worded.	It provides an assurance conclusion. The language of assurance conclusion is negatively worded.

3. SRE 2410 REVIEW OF INTERIM FINANCIAL INFORMATION PERFORMED BY THE INDEPENDENT AUDITOR OF THE ENTITY

What is Interim Financial Information?

Interim financial information is financial information that is prepared and presented in accordance with an applicable financial reporting framework and comprises either a complete or a condensed set of financial statements for a period that is shorter than the entity's financial year.

3.1 Objective of an Engagement to Review Interim Financial Information in Accordance with SRE 2410

The objective of an engagement to review interim financial information is to enable the auditor to express a conclusion whether, on the basis of the review, anything has come to the auditor's attention that causes the auditor to believe that the interim financial information is not prepared, in all material respects, in accordance with an applicable financial reporting framework.

SRE 2410 applies when review of interim financial information is performed by the independent auditor of the financial statements of the entity.

3.2 Agreeing the Terms of the Engagement

The auditor and the client should agree on the terms of the engagement. The agreed terms of the engagement are ordinarily recorded in an engagement letter.

3.3 Understanding the Entity and its Environment including its Internal Control

The auditor should have an understanding of the entity & its environment, including its internal control, as it relates to the preparation of both annual and interim financial information, sufficient to plan and conduct the engagement so as to be able to:

(a) Identify the types of potential material misstatement and consider the likelihood of their occurrence and

(b) Select the inquiries, analytical and other review procedures that will provide the auditor with a basis for reporting whether anything has come to the auditor's attention that causes the auditor to believe that the interim financial information is not prepared, in all material respects, in accordance with the applicable financial reporting framework.

Some of the procedures performed by the auditor to update the understanding of the entity and its environment, including its internal control, ordinarily include the following:

- Reading the documentation, to the extent necessary, of the preceding year's audit and reviews of prior interim period(s) of the current year and corresponding interim period(s) of the prior year.
- Considering any significant risks.
- Reading the most recent annual & comparable prior period interim financial information.
- Considering materiality with reference to the applicable financial reporting framework.
- Considering the nature of any corrected material misstatements and any identified uncorrected immaterial misstatements in the prior year's financial statements.
- Considering significant financial accounting and reporting matters.
- Considering the results of any audit procedures performed with respect to the current year's financial statements.

- Considering the results of any internal audit performed.
- Inquiring of management about the effect of changes in the entity's business activities.
- Inquiring of management about any significant changes in internal control.
- Inquiring of management of the process by which the interim financial information has been prepared and the reliability of the underlying accounting records.

3.4 Inquiries, Analytical and other Review procedures:

The auditor ordinarily performs the following procedures:

- Reading the minutes of the meetings of shareholders, those charged with governance, and other appropriate committees to identify matters that may affect the interim financial information, and inquiring about matters dealt with at meetings for which minutes are not available that may affect the interim financial information.
- Considering the effect, if any, of matters giving rise to a modification of the audit or review report, accounting adjustments or unadjusted misstatements, at the time of the previous audit or reviews.
- Communicating, where appropriate, with other auditors who are performing a review of the interim financial information of the reporting entity's significant components.
- Inquiring of members of management responsible for financial and accounting matters, and others as appropriate about the following:
  - Whether the interim financial information has been prepared and presented in accordance with the applicable financial reporting framework.
  - Whether there have been any changes in accounting principles or in the methods of applying them.
  - Whether any new transactions have necessitated the application of a new accounting principle.
  - Whether the interim financial information contains any known uncorrected misstatements.
  - Unusual or complex situations that may have affected the interim financial information.
  - Significant assumptions that are relevant to the fair value measurement or disclosures and management's intention and ability to carry out specific courses of action on behalf of the entity.

- Whether related party transactions have been appropriately accounted for and disclosed in the interim financial information.
- Significant changes in commitments and contractual obligations.
- Significant changes in contingent liabilities including litigation or claims.
- Compliance with debt covenants.
- Matters about which questions have arisen in the course of applying the review procedures.
- Significant transactions occurring in the last several days of the interim period or the first several days of the next interim period.
- Knowledge of any fraud or suspected fraud.
- Knowledge of any actual or possible non-compliance with laws and regulations.

♦ Applying analytical procedures to the interim financial information designed to identify relationships and individual items that appear to be unusual and that may reflect a material misstatement in the interim financial information.

♦ Reading the interim financial information, and considering whether anything has come to the auditor's attention that causes the auditor to believe that the interim financial information is not prepared, in all material respects, in accordance with the applicable financial reporting framework.

A review of interim financial information ordinarily does not require corroborating the inquiries about litigation or claims.

The auditor may obtain evidence that the interim financial information agrees or reconciles with the underlying accounting records by tracing the interim financial information to:

(a) The accounting records, such as the general ledger, or a consolidating schedule that agrees or reconciles with the accounting records; and

(b) Other supporting data in the entity's records as necessary.

The auditor should inquire whether management has identified all events up to the date of the review report that may require adjustment to or disclosure in the interim financial information.

3.5 Evaluation of Misstatements

The auditor should evaluate, individually and in the aggregate, whether uncorrected misstatements that have come to the auditor's attention are material to the interim financial information.

Misstatements which come to the auditor's attention, including inadequate disclosures, are evaluated individually and in the aggregate to determine whether a material adjustment is required to be made to the interim financial information for it to be prepared, in all material respects, in accordance with the applicable financial reporting framework.

The auditor exercises professional judgment in evaluating the materiality of any misstatements that the entity has not corrected.

3.6 Management representations

The auditor should obtain written representation from management that:

(a) It acknowledges its responsibility for the design and implementation of internal control to prevent and detect fraud and error

(b) The interim financial information is prepared and presented in accordance with the applicable financial reporting framework

(c) It believes the effect of those uncorrected misstatements aggregated by the auditor during the review are immaterial, both individually and in the aggregate.

(d) It has disclosed to the auditor all significant facts relating to any frauds.

(e) It has disclosed to the auditor the results of its assessment of the risks.

(f) It has disclosed to the auditor all known actual or possible non-compliance.

(g) It has disclosed to the auditor all significant events that have occurred subsequent to the balance sheet date and through to the date of the review report.

3.7 Auditor's Responsibility for Accompanying Information

Similar to SA 720 Chapter 7

3.8 Communication

When, as a result of performing the review of interim financial information, a matter comes to the auditor's attention that causes the auditor to believe that it is necessary to make a material adjustment to the interim financial information for it to be prepared, in all material respects, in accordance with the applicable financial reporting framework, the auditor should communicate this matter as soon as practicable to the appropriate level of management.

When, in the auditor's judgment, management does not respond appropriately within a reasonable period of time, the auditor should inform those charged with governance. The communication is made as soon as practicable, either orally or in writing. The auditor's decision whether to communicate orally or in writing is affected by factors such as the nature, sensitivity and significance of the matter to be communicated and the timing of such communications. If the information is communicated orally, the auditor documents the communication.

When, in the auditor's judgment, those charged with governance do not respond appropriately within reasonable period, the auditor should consider:

(a) Whether to modify the report or

(b) The possibility of withdrawing from the engagement and

(c) The possibility of resigning from the appointment to audit the annual financial statements

When, as a result of performing the review of interim financial information, a matter comes to the auditor's attention that causes the auditor to believe in the existence of fraud or noncompliance by the entity with laws and regulations, the auditor should communicate the matter as soon as practicable to the appropriate level of management. The determination of which level of management is the appropriate one is affected by the likelihood of collusion or the involvement of a member of management. The auditor also considers the need to report such matters to those charged with governance and considers the implication for the review.

3.9 Reporting the Nature, Extent & Results of the Review of Interim Financial Information

(a)	An appropriate title.
(b)	An addressee, as required by the circumstances of the engagement.
(c)	Identification of the interim financial information reviewed, including identification of the title of each of the statements contained in the complete or condensed set of financial statements and the date and period covered by the interim financial information.
(d)	If the interim financial information comprises a complete set of general-purpose financial statements prepared in accordance with a financial reporting framework designed to achieve fair presentation, a statement that management is responsible for the preparation and fair presentation of the interim financial information in accordance with the applicable financial reporting framework.
(e)	In other circumstances, a statement that management is responsible for the preparation and presentation of the interim financial information in accordance with the applicable financial reporting framework.
(f)	A statement that the auditor is responsible for expressing a conclusion on the interim financial information based on the review.
(g)	A statement that the review of the interim financial information was conducted in accordance with Standard on Review Engagements (SRE) 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity," and a statement that that such a review consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.
(h)	A statement that a review is substantially less in scope than an audit conducted in accordance with Standards on Auditing and consequently does not enable the auditor to obtain assurance that the auditor would become aware of all significant matters that might be identified in an audit and that accordingly no audit opinion is expressed.
(i)	If the interim financial information comprises a complete set of general purpose financial statements prepared in accordance with a financial reporting framework designed to achieve fair presentation, a conclusion as to whether anything has come to the auditor's attention that causes the auditor to believe that the interim

financial information does not give a true and fair view, or does not present fairly, in all material respects, in accordance with the applicable financial reporting framework.

(j) In other circumstances, a conclusion as to whether anything has come to the auditor's attention that causes the auditor to believe that the interim financial information is not prepared, in all material respects, in accordance with the applicable financial reporting framework.

(k) The date of the report.

(l) Place of Signature.

(m) The auditor's signature and membership number assigned by the Institute of Chartered Accountants of India (ICAI).

(n) The Firm's registration number of the member of the Institute, wherever applicable, as allotted by ICAI.

Besides, UDIN has also to be generated and stated for review engagement as it is also in nature of an assurance engagement. UDIN has to be stated for engagements performed in accordance with SRE 2400 or SRE 2410.

3.10 Departure from the Applicable Financial Reporting Framework

The auditor should express qualified or adverse conclusion when a matter has come to the auditor's attention that causes the auditor to believe that a material adjustment should be made to the interim financial information for it to be prepared, in all material respects, in accordance with the applicable financial reporting framework.

If matters have come to the auditor's attention that cause the auditor to believe that the interim financial information is or may be materially affected by a departure from the applicable financial reporting framework, and management does not correct the interim financial information, the auditor modifies the review report.

The modification describes the nature of the departure and, if practicable, states the effects on the interim financial information. If the information that the auditor believes is necessary for adequate disclosure is not included in the interim financial information, the auditor modifies the review report and, if practicable, includes the necessary information in the review report. The modification to the review report is ordinarily accomplished by adding an explanatory paragraph to the review report and qualifying the conclusion.

When the effect of the departure is so material and pervasive to the interim financial information that the auditor concludes a qualified conclusion is not adequate to disclose the misleading or incomplete nature of the interim financial information, the auditor expresses an adverse conclusion.

3.11 Limitation on Scope

3.11.1. Limitation on Scope Imposed by Management

The auditor does not accept an engagement to review the interim financial information if the auditor's preliminary knowledge of the engagement circumstances indicates that the auditor would be unable to complete the review because there will be a limitation on the scope of the auditor's review imposed by the management of the entity.

If, after accepting the engagement, management imposes a limitation on the scope of the review, the auditor requests the removal of that limitation. If management refuses to do so, the auditor is unable to complete the review and express a conclusion. In such cases, the auditor communicates, in writing, to the appropriate level of management and those charged with governance the reason why the review cannot be completed. Nevertheless, if a matter comes to the auditor's attention that causes the auditor to believe that a material adjustment to the interim financial information is necessary for it to be prepared, in all material respects, in accordance with the applicable financial reporting framework, the auditor communicates such matters.

The auditor also considers the legal and regulatory responsibilities, including whether there is a requirement for the auditor to issue a report. If there is such a requirement, the auditor disclaims a conclusion, and provides in the review report the reason why the review cannot be completed. However, if a matter comes to the auditor's attention that causes the auditor to believe that a material adjustment to the interim financial information is necessary for it to be prepared, in all material respects, in accordance with the applicable financial reporting framework, the auditor also communicates such a matter in the report.

3.11.2 Other Limitations on Scope

A limitation on scope may occur due to circumstances other than a limitation on scope imposed by management. In such circumstances, the auditor is ordinarily unable to complete the review and express a conclusion. There may be, however, some rare circumstances where the limitation on the scope of the auditor's work is clearly confined to one or more specific matters that, while material, are not in the auditor's judgment pervasive to the interim financial information. In such circumstances, the auditor modifies the review report by indicating that, except for the matter which is described in an explanatory paragraph to the review report, the review was conducted in accordance with this SRE, and by qualifying the conclusion.

The auditor may have expressed a qualified opinion on the audit of the latest annual financial statements because of a limitation on the scope of that audit. The auditor considers whether that limitation on scope still exists and, if so, the implications for the review report.

3.12 Going Concern and Significant Uncertainties

If, as a result of inquiries or other review procedures, a material uncertainty relating to an event or condition comes to the auditor's attention that may cast significant doubt on the entity's ability to continue as a going concern, and adequate disclosure is made in the interim financial information the auditor modifies the review report by adding an emphasis of matter paragraph.

The auditor may have modified a prior audit or review report by adding an emphasis of matter paragraph to highlight a material uncertainty relating to an event or condition that may cast significant doubt on the entity's ability to continue as a going concern. If the material uncertainty still exists and adequate disclosure is made in the interim financial information, the auditor modifies the review report on the current interim financial information by adding a paragraph to highlight the continued material uncertainty.

If a material uncertainty that casts significant doubt about the entity's ability to continue as a going concern is not adequately disclosed in the interim financial information, the auditor should express a qualified or adverse conclusion, as appropriate. The report should include specific reference to the fact that there is such a material uncertainty.

3.13 Other Considerations

The terms of the engagement include management's agreement that where any document containing interim financial information indicates that such information has been reviewed by the entity's auditor, the review report will also be included in the document. If management has not included the review report in the document, the auditor considers seeking legal advice to assist in determining the appropriate course of action in the circumstances.

If the auditor has issued a modified review report and management issues the interim financial information without including the modified review report in the document containing the interim financial information, the auditor considers seeking legal advice to assist in determining the appropriate course of action in the circumstances, and the possibility of resigning from the appointment to audit the annual financial statements.

11. PROSPECTIVE FINANCIAL INFORMATION AND OTHER ASSURANCE SERVICES

1. INTRODUCTION

1.1 Standards on Assurance Engagements

An assurance engagement may relate to examination of subject matters other than examination of financial statements prepared on basis of "historical financial information". In such type of assurance engagements, examination may relate to prospective financial information or to providing assurance regarding non-financial matters like design and operation of internal control in an entity.

Standards on Assurance Engagements deal with responsibilities of professional accountants in assurance engagements dealing such matters. The level of assurance provided by these Standards on Assurance Engagements is moderate.

2. SAE 3400 THE EXAMINATION OF PROSPECTIVE FINANCIAL INFORMATION

What is Prospective financial information?

"Prospective financial information's" Financial information based on:

- Assumptions about events that may occur in the future and
- Possible actions by an entity.

What is Forecast?

Forecast means Prospective Financial Information prepared on the basis of:

- Assumptions as to future events which management expects to take place and
- The actions management expects to take as of the date the information is prepared.

(Best- estimate assumptions- An assumption that reflects anticipated experience with no provision for risk of adverse deviation.).

What is Projection?

Prospective Financial Information prepared on the basis of:

- Hypothetical assumptions about future events and management actions which are not necessarily expected to take place, such as when some entities are in a start-up phase or are considering a major change in the nature of operations; or

- A mixture of best-estimate and hypothetical assumptions (imagined or suggested)

2.1 Scope of SAE-3400

The purpose of this Standard on Assurance Engagement (SAE) is to establish standards & provide guidance on engagements to examine & report on prospective financial information including examination procedures for best-estimate & hypothetical assumptions.

The term "auditor" is used throughout this SAE when describing services involving examination of prospective financial information. Such reference is not intended to imply that a member performing such services need necessarily be the statutory auditor of the entity's financial statements.

2.2 Nature of Assurance Regarding Prospective Financial Information

Prospective financial information relates to events and actions that have not yet occurred and might not occur. While evidence may be available to support the assumptions on which the prospective financial information is based, such evidence is itself generally future- oriented and, therefore, speculative in nature, as distinct from the evidence ordinarily available in the examination of historical financial information. Therefore, an opinion as to whether the results shown in the prospective financial information will be achieved cannot be expressed.

2.3 Responsibility of Preparation and Presentation of Prospective Financial Information

Management is responsible for the preparation and presentation of the prospective financial information including the:

- Identification and disclosure of Prospective Financial Information;
- Explaining the basis of forecast;
- Underlying assumptions.

2.4 Duties of Member who is Examining the Prospective Financial Information

In an engagement to examine prospective financial information, the audit should obtain sufficient appropriate evidence as to whether:

(a) management's best-estimate assumptions on which the prospective financial information is based **are not unreasonable** and, in the case of hypothetical assumptions, such **assumptions are consistent with the purpose of the information;**

(b) the prospective financial information is **properly prepared on the basis of the assumptions;**

(c) the prospective financial information is **properly presented** and all material assumptions are adequately disclosed, including a clear indication as to whether they are best-estimate assumptions or hypothetical assumptions; and

(d) the prospective financial information is prepared **on a consistent basis** with historical financial statements, using appropriate accounting principles.

While examining prospective financial information, principles laid down in other Standards on Auditing should be applied to the extent practicable.

2.5 Acceptance of Engagement: Precautions to be taken by Auditor before Accepting such an Engagement

Before accepting an engagement to examine prospective financial information, the auditor would consider, amongst other things:

Acceptance of Engagement

- **The intended use of the information;**
- **Whether the information will be for general or limited distribution;**
- **The nature of the assumptions, that is, whether they are best-estimates or hypothetical assumptions;**
- **The elements to be included in the information; and**
- **The period covered by the information.**

2.6 Examination Procedures

When determining the nature, timing and extent of examination procedures, the following matters should be considered such as:

(a) the knowledge obtained during any previous engagements

(b) management's competence regarding the preparation of prospective financial information

(c) the likelihood of material misstatement

(d) the extent to which the prospective financial information is affected by the management's judgment

(e) the sources of information considered by the management for the purpose, their adequacy, reliability of the underlying data, including data derived from third parties, such as industry statistics, to support the assumptions

(f) the stability of entity's business and

(g) the engagement team's experience with the business and the industry in which the entity operates and with reporting on prospective financial information

In performing these procedures, source and reliability of the evidence supporting management's best-estimate assumptions needs to be assessed. Such evidence may be available from varied sources like entity's budgets, debt agreements, industry publications etc.

2.7 Presentation and Disclosure

When assessing the presentation and disclosure of the prospective financial information and the underlying assumptions, in addition to the specific requirements of any relevant statutes, regulations as well as the relevant professional pronouncements, it needs to be considered whether: -

(a) the presentation of prospective financial information is informative and not misleading

(b) the accounting policies are clearly disclosed in the notes to the prospective financial information:

(c) the assumptions are adequately disclosed in the notes to the prospective financial information. It needs to be clear whether assumptions represent management's best-estimates or are hypothetical and, when assumptions are made in areas that are material and are subject to a high degree of uncertainty, this uncertainty and the resulting sensitivity of results needs to be adequately disclosed.

(d) the date as of which the prospective financial information was prepared is disclosed.

Management needs to confirm that the assumptions are appropriate as of this date, even though the underlying information may have been accumulated over a period of time.

(e) the basis of establishing points in a range is clearly indicated and the range is not selected in a biased or misleading manner when results shown in the prospective financial information are expressed in terms of a range and

(f) if there is any change in the accounting policy of the entity from that disclosed in the most recent historical financial statements, whether reason for the change & the effect of such change on the prospective financial information has been adequately disclosed.

2.8 Report on Examination of Prospective Financial Information

The report for an examination of prospective financial information should contain the following:

(a) Title

(b) Addressee

(c) Identification of the prospective financial information

(d) Reference to the Standards on Auditing applicable to the examination of prospective financial information

(e) Statement that management is responsible for the prospective financial information including the underlying assumptions

(f) When applicable, a reference to the purpose and/or restricted distribution of the prospective financial information

(g) Statement that the examination procedures included examination, on a test basis, of evidence supporting the assumptions, amounts and other disclosures in the forecast or projection

(h) Statement of negative assurance as to whether the assumptions provide a reasonable basis for the prospective financial information

(i) Opinion as to whether the prospective financial information is properly prepared on the basis of the assumptions and is presented in accordance with the relevant financial reporting framework.

(j) Appropriate caveats concerning the achievability of the results indicated by the prospective financial information

(k) Date of report (which should be the date procedures have been completed)

(l) Place of signature and

(m) Signature

♦ **State that:-**

- Actual results are likely to be different from the prospective financial information since anticipated events frequently do not occur as expected and the variation could be material. Likewise, when the prospective financial information is expressed as a range, it would be stated that there can be no assurance that actual results will fall within the range and
- In the case of a projection, the prospective financial has been prepared for (intended use), using a set of assumptions that include hypothetical assumptions about future events and management's actions that are not necessarily expected to occur. Consequently, readers are cautioned that the prospective financial information should not be used for purposes other than the abovementioned intended use.

When it is believed that the presentation and disclosure of the prospective financial information is not adequate, a qualified or adverse opinion in the report on the prospective financial information should be expressed or withdrawal from engagement should be made as appropriate.

When it is believed that one or more significant assumptions do not provide a reasonable basis for the prospective financial information prepared on the basis of best-estimate assumptions or that one or more significant assumptions do not provide a reasonable basis for the prospective financial information given the hypothetical assumptions, an adverse opinion setting out the reasons in the report on the prospective financial information should be expressed, or withdrawal from the engagement should be made.

When the examination is affected by conditions that preclude application of one or more procedures considered necessary in the circumstances, either withdrawal from the engagement or disclaimer of the opinion and describing the scope limitation in the report on the prospective financial information is considered.

3. SAE 3402 Assurance Reports on Controls at a Service Organisation

3.1 Scope of SAE 3402

SAE 3402 applies only when the service organization is responsible for, or otherwise able to make an assertion about, the suitable design of controls. It does not deal with assurance engagements:

(a) To report only on whether controls at a service organization operated as described or

(b) To report only on controls at a service organization other than those related to a service that is likely to be relevant to user entities' internal control as it relates to financial reporting.

3.1.1 What is a Service Organisation?

Service organization refers to a third-party organization (or segment of a third-party organization) that provides services to user entities that are likely to be relevant to user entities internal control as it relates to financial reporting. User entity refers to an entity that uses a service organization.

3.1.2 User Auditor and Service Auditor

User auditor refers to an auditor who audits and reports on the financial statements of a user entity.

Service auditor refers to a professional accountant in public practice who, at the request of the service organization, provides an assurance report on controls at a service organization.

3.2 Objectives of Service Auditor in Accordance with SAE 3402

The objectives of the service auditor are-:

(a) To obtain reasonable assurance about whether, in all material respects, base suitable criteria:-

(i) The service organization's description of its system fairly presents the system as designed and implemented throughout the specified period (or in the case of a type 1 report, as at a specified date)

(ii) The controls related to the control objectives stated in the service organization's description of its system were suitably designed throughout the specified period (or in the case of a type 1 report, as at a specified date)

(iii) Where included in the scope of the engagement, the controls operated effectively to provide reasonable assurance that the control objectives stated in the service organization's description of its system were achieved throughout the specified period.

(b) To report on the matters in (a) above in accordance with the service auditor's findings.

3.3 Type 1 Report & Type 2 Report

Type 1 report is a report that comprises:	**Type 2 report is a** report that comprises:
(i) The service organization's description of its system;	(i) The service organization's description of its system
(ii) A written assertion by the service organization that, in all material respects, and based on suitable criteria:	(ii) A written assertion by the service organization that, in all material respects, and based on suitable criteria:
a. The description fairly presents the service organization's system as designed and implemented at the specified date	a. The description fairly presents the service organization's system as designed and implemented throughout the specified period
b. The controls related to the control objectives stated in the service organization's description of its system were suitably designed as at the specified date and	b. The controls related to the control objectives stated in the service organization's description of its system were suitably designed throughout the specified period and c. The controls related to the control objectives stated in the service organization's description of its system operated effectively throughout the specified period and

(iii) A service auditor's assurance report that conveys reasonable assurance about the matters referred to in (ii)	(iii) A service auditor's assurance report that: (a) Conveys reasonable assurance about the matters in (ii) and (b) Includes a description of the tests of controls and the results thereof.
Type 1 report is a report on the description and design of controls at a service organization whereas type 2 report is a report on the description, design and operating effectiveness of controls at a service organization.	

3.4 How such an Engagement is proceeded with?

1. **Compliance with ethical requirements:** The service auditor shall comply with relevant ethical requirements, including those pertaining to independence, relating to assurance engagements.

2. **Determination of Management and those charged with governance and communication with them:** The service auditor shall inquire of, request representations from, communicate with, or otherwise interact with the service organization wherever required.

3. **Acceptance and changes in terms of engagement:** Before, accepting such an engagement, it has to be ensured by service auditor that necessary capabilities and competence to carry out such engagement are possessed by him.

4. **Assessing of suitability of the Criteria:** The service auditor shall assess whether the service organization has used suitable criteria in preparing the description of its system, in evaluating whether controls are suitably designed, and, in the case of a type 2 reports, in evaluating whether controls are operating effectively.

5. **Determination of Materiality:** When planning and performing the engagement, the service auditor shall consider materiality with respect to the fair presentation of the description, the suitability of the design of controls and, in the case of a type 2 report, the operating effectiveness of controls.

6. **Obtaining an understanding of the Service organization's system:** The service Auditor shall obtain an understanding of the service organization's system, including controls that are included in the scope of engagement.

7. **Obtaining evidence regarding the description:** The service auditor shall obtain and read the service organization's description of its system and evaluate whether those aspects of the description included in the scope of engagement are fairly presented.

8. **Obtaining evidence regarding the design of controls:** The service auditor shall determine which of the controls at the service organization are necessary to achieve the control objectives stated in the service organization's description of its system and shall assess whether those controls were suitably designed.

9. **Obtaining evidence regarding operating effectiveness of control:** When providing a type 2 report, the service auditor shall test those controls that the service auditor has determined are necessary to achieve the control objectives stated in the service organization's description of its system, and assess their operating effectiveness throughout the period.

10. **Understanding the internal audit function:** If the service organization has an internal audit function, the service auditor shall obtain an understanding of the nature of the responsibilities of the internal audit function and of the activities performed in order to determine whether the internal audit function is likely to be relevant to the engagement in order for the service auditor to use specific work of the internal auditors.

11. **Asking for Written Representations:**

(a) That reaffirm the assertion accompanying the description of the system

(b) That it has provided the service auditor with all relevant information and access agreed to and

(c) That it has disclosed to the service auditor any of the following of which it is aware:-

(i) Non-compliance with laws and regulations, fraud, or uncorrected deviations.

(ii)	Design deficiencies in controls
(iii)	Instances where controls have not operated as described and
(iv)	Any events subsequent to the period covered.
12.	**Subsequent Events:** The service auditor shall inquire whether the service organization is aware of any events subsequent to the period covered by the service organization's description of its system up to the date of the service auditor's assurance report that could have a significant effect on the service auditor's assurance report.
3.5	**Reporting**
(a)	A title
(b)	An addressee.
(c)	Identification of:
(i)	The service organization's description of its system.
(ii)	Those parts of the service organization's description of its system, if any, that are not covered by the service auditor's opinion.
(iii)	If the description refers to the need for complementary user entity controls, a statement that the service auditor has not evaluated the suitability of design or operating effectiveness of complementary user entity controls.
(iv)	If services are performed by a subservice organization, the nature of activities performed by the subservice organization.
(d)	Identification of the criteria, and the party specifying the control objectives.
(e)	A statement that the report and, in the case of a type 2 report, the description of tests of controls are intended only for user entities.
(f)	A statement that the service organization is responsible for: -
(i)	Preparing the description of its system
(ii)	Providing the services covered by the service organization's description of its system;
(iii)	Stating the control objectives.
(iv)	Designing and implementing controls to achieve the control objectives.
(g)	A statement that the service auditor's responsibility is to express an opinion.
(h)	A statement that the engagement was performed in accordance with SAE 3402.

(i)	A summary of the service auditor's procedures to obtain reasonable assurance & a statement of the service auditor's belief that the evidence obtained is sufficient and appropriate to provide a basis for the service auditor's opinion.
(j)	A statement of the limitations of controls.
(k)	The service auditor's opinion, expressed in the positive form, on whether, in all material respects, based on suitable criteria:
(i)	In the case of a type 2 report:-
a.	The description fairly presents the service organization's system that had been designed and implemented throughout the specified period;
b.	The controls related to the control objectives stated in the service organization's description of its system were suitably designed throught the specified period; 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 specified period.
(ii)	In the case of a type 1 report:-
a.	The description fairly presents he service organization's system that had been designed and implemented as at the specified date and
b.	The controls related to the control objectives stated in the service organization's description of its system were suitably designed as at the specified date.
(l)	The date of the service auditor's assurance report, which shall be no earlier than the date on which the service auditor has obtained sufficient appropriate evidence on which to base the opinion.
(m)	Signature-The report should be signed by the practitioner.
(n)	The place of signature - the report should name specific location, which is ordinarily the city where the report is signed.
	Modified Opinions
	If the service auditor concludes that:
(a)	The service organization's description does not fairly present, in all material respects, the system as designed and implemented;
(b)	The controls related to the control objectives stated in the description were not

suitably designed, in all material respects

(c) In the case of a type 2 report, the controls tested, which were those necessary to provide reasonable assurance that the control objectives stated in the service organization's description of its system were achieved, did not operate effectively, in all material respects or

(d) The service auditor is unable to obtain sufficient appropriate evidence, the service auditor's opinion shall be modified, and the service auditor's assurance report shall contain a clear description of all the reasons for the modification.

4. SAE 3420 ASSURANCE ENGAGEMENTS TO REPORT ON THE COMPILATION OF PRO FORMA FINANCIAL INFORMATION INCLUDED IN A PROSPECTUS

What is Pro forma financial information?

Pro forma financial information refers to financial information shown together with adjustments to illustrate the impact of an event or transaction on unadjusted financial information as if the event had occurred or the transaction had been undertaken at an earlier date selected for purposes of the illustration.

4.1 Objectives in Accordance with SA 3420

The objectives of the practitioner in accordance with SA 3420 are:-

(a) To obtain reasonable assurance about whether the pro forma financial information has been compiled, in all material respects, by the responsible party on the basis of the applicable criteria and

(b) To report in accordance with the practitioner's findings.

4.2 Compilation of Pro forma financial information

Steps involved in this process include:

- Identifying the source of the unadjusted financial information to be used in compiling the pro forma financial information, and extracting the unadjusted financial information from that source
- Making pro forma adjustments to the unadjusted financial information for the purpose for which the pro forma financial information is presented and

- Presenting the resulting pro forma financial information with accompanying disclosures.

4.3 Nature of the Practitioner's Responsibility

In such an engagement performed under this SAE, the practitioner has no responsibility to compile the pro forma financial information for the entity. Such responsibility rests with the responsible party. The practitioner's sole responsibility is to report on whether the pro forma financial information has been compiled, in all material respects, by the responsible party on the basis of the applicable criteria.

4.4 Steps involved in such an Engagement

- Engagement acceptance
- Planning and performing the Engagement
- Written Representations
- Forming the opinion
- Preparing the assurance report

4.4.1 Engagement Acceptance

(a) Determine that the practitioner has the capabilities and competence to perform the engagement

(b) On the basis of a preliminary knowledge of the engagement circumstances and discussion with the responsible party, determine that the applicable criteria are suitable and that it is unlikely that the pro forma financial information will be misleading for the purpose for which it is intended.

(c) Evaluate the wording of the opinion prescribed by the relevant law or regulation, if any, to determine that the practitioner will likely be able to express the opinion so prescribed based on performing the procedures specified in this SAE

(d) Where the sources from which the unadjusted financial information and any acquiree or divestee financial information have been extracted have been audited or reviewed and a modified audit opinion or review conclusion has been expressed, or the report contains an Emphasis of Matter paragraph, consider whether or not the relevant law or regulation permits the use of, or reference in the practitioner's report to, the *modified audit opinion or review conclusion or the report containing the Emphasis of Matter paragraph with respect to such sources.*

(e) *If the entity's historical financial information has never been audited or reviewed, consider whether the practitioner can obtain a sufficient understanding of the entity and its accounting and financial reporting practices to perform the engagement*

(f) *If the event or transaction includes an acquisition and the acquiree's historical financial information has never been audited or reviewed, consider whether the practitioner can Obtain a sufficient understanding of the acquire and its accounting and financial reporting practices to perform the engagement and*

(g) *Obtain the agreement of the responsible party that it acknowledges and understands its responsibility for:*

Agreement of the Responsible Part:

(i) *Adequately disclosing and describing the applicable criteria to the intended users if users if these are not publicly available*

(ii) *Compiling the pro forma financial information on the basis of the applicable criteria and*

(iii) *Providing the practitioner with:*

a. *Access to all information*

b. *Additional information that the practitioner may request from the responsible party*

c. *Access to those within the entity and the entity's advisors from whom the practitioner determines it necessary to obtain evidence*

d. *When needed for purposes of the engagement, access to appropriate individuals within the acquire (s) in business combination.*

4.4.2 Planning and Performing the Engagement

- *The practitioner shall assess whether the applicable criteria are suitable, as required by the Framework for Assurance Engagements.*
- *When planning and performing the engagement, the practitioner shall consider materiality with respect to evaluating whether the pro forma financial information has been compiled, in all material respects, on the basis of the applicable criteria.*
- *An understanding of how the responsible party has compiled the pro forma financial Information and other engagement circumstances*

- The practitioner shall obtain evidence about the appropriateness of the source from which the unadjusted financial information has been extracted
- If there is no audit or review report on the source from which the unadjusted financial information has been extracted, the practitioner shall perform procedures to be satisfied that the source is appropriate.
- The practitioner shall determine whether the responsible party has appropriately extracted the unadjusted financial information from the source.
- The practitioner shall obtain evidence about the appropriateness of the pro forma adjustments.

In relation to unadjusted financial information, Pro forma adjustments include:

(a) Adjustments to unadjusted financial information that illustrate the impact of a significant event or transaction as if the event had occurred or the transaction had been undertaken at an earlier date selected for purposes of the illustration and

(b) Adjustments to unadjusted financial information that are necessary for the pro forma financial information to be compiled on a basis consistent with the applicable financial reporting framework of the reporting entity and its accounting policies under that framework.

- The practitioner shall evaluate the presentation of pro forma financial information.
- The practitioner shall read the other information included in the Prospectus containing the pro forma financial information to identify material inconsistencies, if any, with pro forma financial information.

4.4.3 Written Representations

The practitioner shall request written representations from the responsible party that:-

(a) In compiling the pro forma financial information, the responsible party has identified all appropriate pro forma adjustments necessary to illustrate the impact of the event or transaction at the date or for the period of the illustration and

(b) The pro forma financial information has been compiled, in all material respects, on the basis of the applicable criteria.

4.4.4 Opinion

4.4.4.1 Unmodified Opinion

The practitioner shall express an unmodified opinion when the practitioner concludes that the pro forma financial information has been compiled, in all material respects, by the responsible party on the basis of the applicable criteria.

4.4.4.2 Modified Opinion

(a) Where the relevant law or regulation precludes publication of a prospectus that contains a modified opinion with regard to whether the pro forma financial information has been compiled, in all material respects, on the basis of the applicable criteria and the practitioner concludes that a modified opinion is nevertheless appropriate in accordance with the Framework for Assurance Engagements, the practitioner shall discuss the matter with the responsible party.

If the responsible party does not agree to make the necessary changes, the practitioner shall:-

- Withdraw from the engagement or
- Consider seeking legal advice

(b) Where the relevant law or regulation may not preclude publication of a prospectus that contains a modified opinion with regard to whether the pro forma financial information has been compiled, in all material respects, on the basis of the applicable criteria and the practitioner determines that a modified opinion is appropriate in accordance with the Framework for Assurance Engagements, the practitioner shall apply the requirements in the Framework for Assurance Engagements regarding modified opinions.

4.4.4.3 Emphasis of Matter Paragraph

Similar to SA 706 Chapter 7

4.4.5 Preparing the Assurance Report

The practitioner's report shall include the following basic elements: -

Basic elements of Assurance Report

(a)	A title that clearly indicates that the report is an independent assurance report
(b)	An addressee(s), as agreed in the terms of engagement
(c)	**Introductory paragraphs that identify:**
(i)	The pro forma financial information
(ii)	The source from which the unadjusted financial information has been extracted and whether or not an audit or review report on such a source has been published
(iii)	The period covered by, or the date of, the pro forma financial information and
(iv)	A reference to the applicable criteria on the basis of which the responsible party has performed the compilation of the pro forma financial information, and the source of the criteria
(d)	A statement that the responsible party is responsible for compiling the pro forma financial information on the basis of the applicable criteria
(e)	**A description of the practitioner's responsibilities, including statements that: -**
(i)	The practitioner's responsibility is to express an opinion
(ii)	For purposes of this engagement, the practitioner is not responsible for updating or reissuing any reports or opinions on any historical financial information used in compiling the pro forma financial information.
(iii)	The purpose of pro forma financial information included in a prospectus is solely to illustrate the impact of a significant event or transaction on unadjusted financial information of the entity as if the event had occurred or the transaction had been undertaken at an earlier date selected for purposes of the illustration. Accordingly, the practitioner does not provide any assurance that the actual outcome of the event or transaction at that date would have been as presented
(f)	A statement that the engagement was performed in accordance with SAE 3420.
(g)	Statements that:-
(i)	A reasonable assurance engagement to report on whether the pro forma financial information has been compiled, in all material respects, on the basis of the applicable criteria involves performing procedures to assess whether the applicable criteria used by the responsible party in the compilation of the pro forma financial information provide a reasonable basis for presenting the significant effects directly attributable to the event or transaction and to obtain sufficient appropriate evidence about whether:-

(a)	The related pro forma adjustments give appropriate effect to those criteria; and
(b)	The pro forma financial information reflects the proper application of those adjustments to the unadjusted financial information
(ii)	The procedures selected depend on the practitioner's judgment, having regard to the practitioner's understanding of the nature of the entity, the event or transaction in respect of which the pro forma financial information has been complied, and other relevant engagement circumstances and
(iii)	The engagement also involves evaluating the overall presentation of the pro forma financial information
(h)	Unless otherwise required by law or regulation, the practitioner's opinion using one of the following phrases, which are regarded as being equivalent:-
(i)	The pro forma financial information has been complied, in all material respects, on the basis of the applicable criteria or
(ii)	The pro forma financial information has been properly complied on the basis stated.
(i)	The practitioner's signature
(j)	The date of the report and
(k)	The place of signature.